FATF-X

FINANCIAL ACTION TASK FORCE ON MONEY LAUNDERING

ANNUAL REPORT 1998-1999

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SUMMARY

1. Japan chaired the tenth round of the Financial Action Task Force on Money Laundering (FATF). Major achievements of the 1998-1999 round included the completion of the second set of mutual evaluations of the anti-money laundering measures taken by its members, and launching the enlargement of the FATF membership. All FATF members have now been subject to two in-depth examinations of their anti-money laundering regimes. Three countries (Argentina, Brazil and Mexico) will be invited to join the FATF as observers in September 1999.

2. The FATF also continued its task of refining anti-money laundering measures in several areas (accounting professions and associated rules, strengthening international co-operation, consideration of how anti-money laundering systems can contribute to dealing effectively with tax related crimes). In this respect, an Interpretative Note to Recommendation 15 was adopted in order to close the "fiscal excuse" in the reporting of suspicious transactions. Important work on the problems raised by non-cooperative countries or territories in the combat of money laundering was also launched during the year. In addition, the Task Force conducted its annual broad-ranging review of money laundering trends and techniques.

3. As in previous rounds, the Task Force devoted a considerable part of its work to the monitoring of members' implementation of the forty Recommendations on the basis of the self-assessment and mutual evaluation procedures. The 1998-1999 self-assessment exercise showed that members had continued to make progress in implementing the forty Recommendations. Furthermore, the mutual evaluation procedure, which provides for a thorough examination of the counter-measures in place and their effectiveness, continues to be an irreplaceable monitoring mechanism. All FATF members have now been examined in the second round of mutual evaluations. Summaries of the twelve mutual evaluation examinations (Spain; Finland; Luxembourg; Ireland; Hong Kong, China; New Zealand; Iceland; Singapore; Portugal; Turkey; Aruba and the Netherlands Antilles[1]) which were conducted during FATF-X are contained in Part I of the report. In January 1999, the FATF carried out a mission to the Gulf Cooperation Council's headquarters in Riyadh to discuss how to improve the implementation of effective anti-money laundering systems among the GCC members.

4. The assessment of current and future money laundering threats is an essential part of the FATF's work. The annual survey of money laundering typologies[2] focused on a number of major issues: the Euro currency unit and large denomination banknotes; problems associated with offshore financial centres of non-cooperative jurisdictions, including the identification of the beneficial owners of foreign legal entities; challenges posed by new payment technologies; and the potential use of the gold market in money laundering operations. During the round, experts from FATF members and several international organisations continued the work commenced in 1997 on estimating the magnitude of money laundering.

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[1] Aruba and the Netherlands Antilles are separate constituent parts of the Kingdom of the Netherlands which is a member of FATF.

[2] See Annex C.

5. The FATF supported the various activities of other regional and international bodies involved in the fight against money laundering. In this regard, it should be noted that the Caribbean FATF and the Select Committee of the Council of Europe (PC-R-EV) continued to carry out mutual evaluation programmes of the anti-money laundering measures taken by their members. The Asia/Pacific Group on Money Laundering pursued its anti-money laundering activities, notably through two typologies exercises, held in October 1998 and March 1999. In October 1998, the FATF organised an international money laundering Seminar in Athens for the countries of the Black Sea Economic Cooperation.

6. According to the objectives agreed upon in April 1998 by FATF's Ministers, the issue of enlarging FATF membership and the strengthening of the work of FATF-style regional bodies will be pursued in 1999-2000. These essential tasks will be carried out under the Presidency of Portugal, which will commence on 3 July 1999.

INTRODUCTION

7. The Financial Action Task Force was established by the G-7 Summit in Paris in July 1989 to examine measures to combat money laundering. In 1990, the FATF issued forty Recommendations for action against this phenomenon. These were revised in 1996 to reflect changes in money laundering trends. The current membership of the FATF comprises twenty-six governments[3] and two regional organisations,[4] representing the major financial centres of North America, Europe and Asia. The delegations of the Task Force's members are drawn from a wide range of disciplines, including experts from the Ministries of Finance, Justice, Interior and External Affairs, financial regulatory authorities and law enforcement agencies.

8. In July 1998, Japan succeeded Belgium in holding the Presidency of the Task Force for its tenth round of work. Three Plenary meetings were held in 1998-1999, two at the headquarters of the OECD in Paris and one in Tokyo. Two special experts' meetings were held; the first in November 1998 in London to consider trends and developments in money laundering methods and counter-measures and the second in December 1998 to work on the issue of estimating the size of money laundering. Finally, an informal contact meeting took place in January 1999 between the OECD's Committee on Fiscal Affairs (CFA) and the FATF.

9. The FATF co-operates closely with international and regional organisations concerned with combating money laundering. Representatives from the Asia/Pacific Group on Money Laundering (APG), the Caribbean Financial Action Task Force (CFATF), the Council of Europe, the International Monetary Fund (IMF), the Inter-American Drug Abuse Control Commission of the Organisation of American States (OAS/CICAD), Interpol, the International Organisation of Securities Commissions (IOSCO), the Offshore Group of Banking Supervisors (OGBS), the United Nations Office for Drug Control and Crime Prevention (UNODCCP), and the World Customs Organisation (WCO) attended various FATF meetings during the year.

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[3] Australia; Austria; Belgium; Canada; Denmark; Finland; France; Germany; Greece; Hong Kong, China; Iceland; Ireland; Italy; Japan; Luxembourg; the Kingdom of the Netherlands; New Zealand; Norway; Portugal; Singapore; Spain; Sweden; Switzerland; Turkey; the United Kingdom and the United States.

[4] European Commission and Gulf Cooperation Council.

10. Parts I, II and III of the report outline the progress made over the past twelve months in the following three areas:

- monitoring the implementation of anti-money laundering measures by FATF members;
- reviewing money laundering methods and countermeasures; and
- promoting the widest possible international action against money laundering.

I. MONITORING THE IMPLEMENTATION OF ANTI-MONEY LAUNDERING MEASURES

11. FATF members are clearly committed to the discipline of multilateral monitoring and peer review. Therefore, a notable part of FATF's work has continued to focus on monitoring the implementation by its members of the forty Recommendations on the basis of a self-assessment and mutual evaluation procedure. The self-assessment exercise consists of a detailed questionnaire and a question and answer session at the final Plenary meeting. The mutual evaluation procedure provides a comprehensive monitoring mechanism for the examination of the counter-measures in place in member countries and of their effectiveness. Together, they provide the necessary peer pressure for a thorough implementation of the forty Recommendations in members.

A. 1998/1999 SELF-ASSESSMENT EXERCISE

(i) Process

12. In this exercise, each member provides information on the status of its implementation of the forty Recommendations on the basis of two sets of standard questions dealing with legal and financial aspects respectively. This information is then compiled and analysed, and provides the basis for assessing the extent to which the forty Recommendations have been implemented by both individual countries and the group as a whole.

(ii) State of implementation[5]

(a) Legal issues

13. The overall state of implementation is similar to the situation in the previous round, with almost all members being in compliance with a large majority of the Recommendations, though a few areas of non-compliance remain. A significant step was that all members but one have now ratified, and all have fully implemented the money laundering components of the Vienna Convention. In addition, all but two countries have extended the money laundering offence and ancillary measures to a range of serious crimes.

14. In regard to most Recommendations the position is quite satisfactory, though the overall level of compliance will improve considerably when Japan and Singapore extend their drug money laundering offences to serious crimes. Though both countries now have legislation before their parliaments, this needs to be passed and implemented as soon as possible, as it is a real concern that they are out of compliance with more than half of the legal Recommendations. Luxembourg, was notable in 1998-1999

[5] A copy of the summary of compliance with the legal and financial Recommendations is at Annex B.

for extending its money laundering legislation beyond drug trafficking, thus entering into full compliance with all the legal Recommendations. In general, while steady progress continues to be made, weaknesses still remain in relation to the Recommendations dealing with international mutual legal assistance, and increased attention should be paid to rectifying these deficiencies.

15. The weaknesses that existed in 1997-1998 in relation to confiscation and provisional measures, both domestically and pursuant to mutual legal assistance, still exist. In relation to domestic confiscation, twenty-two members are in full compliance, with four in partial compliance, whilst for mutual legal assistance in this area, there are twenty members in full compliance, three which partially comply, and three which remain out of compliance (Canada, Greece and the United States). These figures show only a very slow increase in compliance over the past few years, and there needs to be increased attention by some members to bring themselves into compliance with the relevant Recommendations.

(b) Financial issues

16. Despite the positive performance of a handful of members, the 1998-1999 assessment appears to show little positive progress since last year's survey. Most of the movement from full to partial compliance can be attributed to introduction of the new assessment criteria for non-bank financial institutions (the inclusion of the money transmitter/remittance sector as a key category). On a national basis, Belgium, Iceland, Singapore, Switzerland, and Turkey have made progress in complying with the financial Recommendations since last year.

17. A majority of members comply fully with customer identification requirements as far as banks are concerned (Recommendations 10 and 11), although there is still a significant difference in the coverage of certain types of non-bank financial institutions (NBFIs). Concerns regarding the anonymous passbook savings accounts in Austria still have not been resolved and continue to be pursued through the non-compliance procedures. All members require banks to pay special attention to complex, unusually large transactions; however, their position is far less satisfactory for NBFIs. As in 1997-1998, the reporting of suspicious transactions by banks is mandatory in all members except Canada, and for certain categories of "key" NBFIs in all members except Canada and the United States. In general, the increase in partial compliance with this Recommendation is due, as mentioned above, to the inclusion of money transmitters in this year's analysis. Almost all members are also now in compliance with the closely associated Recommendations 16-18; the decrease in compliance with regard to NBFIs is largely due to the above mentioned changes in stricter assessment criteria.

18. In all members, the supervisory authorities ensure that adequate programmes are set up for banks with an almost similar situation for NBFIs (in all but one member). Only thirteen members, however, have designated authorities to deal with the implementation of the FATF Recommendations in other professions dealing with cash. As has been noted before, it is difficult to assess weaknesses in this area because of the problem of determining which professions should be considered under this Recommendation. Nevertheless, it is clear that a large majority of members have yet to act in this area.

19. Although the retreat from full compliance shown by this year's survey appears largely due to expanded assessment standards, the change still shows that a number of members now need to take additional measures regarding money transmitters if they are to bring themselves into full compliance. Additionally, this year's assessment continues to show the need for certain members to implement additional countermeasures with respect to the banking sector and various categories of non-bank financial institutions as a matter of urgency. As concluded in past surveys, this self-assessment exercise on financial matters has once again confirmed that the emphasis should continue to be placed on extending provisions of the Recommendations to all categories of NBFIs and ultimately to non-financial businesses.

(iii) Summary of performance

20. The overall conclusion from the 1998-1999 self-assessment exercise is that a large majority of members have reached and remained at an acceptable level of compliance with the 1996 Recommendations. A number of members have indeed made significant progress during the preceding year. Nevertheless, some members still must take steps to remedy weaknesses in compliance with the Recommendations on confiscation and provisional measures, and a significant number must act to expand the full range of anti-money laundering measures to non-bank financial institutions and businesses.

B. MUTUAL EVALUATIONS

(i) Generalities

21. The second and major element for monitoring the implementation of the FATF Recommendations is the mutual evaluation process. Each member is examined in turn by the FATF on the basis of a report drawn up by a team of three or four selected experts, drawn from the legal, financial and law enforcement fields of other members. The purpose of this exercise is to provide a comprehensive and objective assessment of the extent to which the country in question has moved forward in implementing effective measures to counter money laundering and to highlight areas in which further progress may still be required.

22. A further twelve mutual evaluations were completed during FATF-X: Spain; Finland; Luxembourg; Ireland; Hong Kong, China; New Zealand; Iceland; Singapore; Portugal; Turkey; Aruba and the Netherlands Antilles (the latter two, which are separate constituent parts of the Kingdom of the Netherlands, were evaluated with the participation of the CFATF). All FATF members have now been subject to the second round of mutual evaluations.

(ii) Summaries of reports

Spain

23. Illicit drug trafficking, forgery, swindling and organised crime are the predominant sources of money which is laundered in Spain. Among the chief money laundering methods within the financial system are: money-changing at banks or bureaux de change, commingling of illicit funds with money generated by lawful activities, and international transfers with incomplete or fictitious data. In addition, the cross-border conveyance of cash as well as investments in the real estate sector through front companies, especially in tourist areas, are also used.

24. Spain's fight against money laundering involves a two-pronged system -- domestic prevention and enforcement -- at home and puts the emphasis on co-operation internationally. Preventive aspects are rooted in Act No. 19/1993 of 28 December, on certain measures for the prevention of money laundering ("the Prevention Act"), and Royal Decree No. 925/1995 of 9 June approving regulations in application of the aforementioned Act which seek to prevent and block money laundering by imposing administrative obligations for reporting and co-operation, on both financial institutions and other non-financial institutions. Act No. 19/1993 also set up the Commission for the Prevention of Money Laundering and Monetary Offences -- the supreme body for co-ordinating the preventive counter-laundering activities of the various bodies with powers in that area -- as well as the Commission's Executive Service (SEPBLAC).

25. With regard to enforcement aspects, approval of the new Spanish Penal Code shifted the definition of the offence of money laundering from one exclusively tied in with goods arising from illicit drug trafficking, to a new one which also includes funds derived from all serious crimes. In addition, special investigative units have been set up within the National Police Corps and the *Guardia Civil* to fight against money laundering in a variety of geographical areas.

26. Having instituted its system later than some other countries, Spain was able, directly, to design a relatively comprehensive mechanism to combat money laundering -- one that more than covers the scope of the FATF Recommendations. However, and for the same reasons, it is still too soon to measure the system's effectiveness exactly, since some provisions, which are theoretically perfect, are only now beginning to be applied.

27. The mechanism's originality warrants note, insofar as a single body, SEPBLAC, concentrates a comprehensive array of know-how conducive to effective and co-ordinated development of all preventive aspects. SEPBLAC, which emerges as the real heart of the preventive arsenal, combines the roles of: the authority that enforces compliance with the Prevention Act by the bodies and persons subject to mandatory reporting, the authority that gathers and analyses reported information on suspicious transactions, and an investigative police unit. SEPBLAC's multidisciplinary nature is certainly an advantage -- one that enables it to exploit the complementarity of its various functions.

28. The originality of the system stems also from the combination of a mechanism for reporting suspicions with a more automatic mechanism having to do with unusual transactions meeting established criteria, such as certain financial transactions with tax havens. Initially focused primarily on money laundering subsequent to illicit drug trafficking, the anti-laundering struggle is beginning to acquire the resources to tackle the phenomenon in connection with other forms of serious crime, including financial offences involving organised crime. The creation, in 1995, of the Special Prosecutor's Office for Corruption-Related Economic Crimes and SEPBLAC's role vis-à-vis that new judicial body are one example of this change.

29. Available statistics, and in particular those on convictions in the specific area of money laundering, do not, however, allow a comprehensive judgement of the effectiveness of this system, which is only recent and could apparently become more effective. Even so, Spain has a comprehensive and original system which more than meets both the spirit and the letter of the FATF Recommendations. It has acquired the legal and functional tools it needs to be effective in detecting and prosecuting money laundering.

Finland

30. In Finland, most of the property acquired by crime is proceeds from financial crime, with the proportion of drug offences as predicate offences for money laundering being approximately 10 % of cases. The majority of proceeds from crime originate from fraud offences, embezzlement, tax fraud, debt offences drug crime, and the avoidance of value added taxes by illegal means such as the importation of gold and GSM-mobile phones to Finland. The most typical method of suspected money laundering cases have been various kinds of account transfers via the banking system, smurfing, and using coupons from betting on the totalizator as proof of the origin of money. There are also a large number of suspect transactions between Finland and Russia, and the origin and purpose of many of these transactions is difficult to investigate. Approximately one-quarter of cases are domestic, with the remainder having a connection abroad. Professional money launderers have not been found and no factual connections to organised crime have been established.

31. The Finnish control policy on money laundering is based on preventing the conversion of

proceeds from crime into seemingly legal property. Emphasis has been placed on increasing the effectiveness of the control system by developing a centralised reporting system, expanding the obligation to report on suspicious transactions to certain categories of non-financial businesses, and supporting the development of money laundering prevention systems in co-operation with neighbouring countries. Since the first evaluation, the most significant change was the enactment of the Act on Preventing and Clearing Money Laundering (the Act) which entered into force on 1 March 1998, and which: (a) established a central unit (the Money Laundering Clearing House)(MLCH) at the National Bureau of Investigation to receive all reports of suspicious transactions; (b) abandoned the two-step structure of the reporting system which had required reports to be made to the Financial Supervision Authority (FSA) and Ministry of Social Affairs and Health, which analysed them before passing them on to the police; and (c) widened the scope of the Act to cover all financial institutions as well as betting agencies, betting on the totalizator, casinos and real estate agents. Other legislation was introduced in 1996 and 1997 to extend anti-money laundering obligations to investment firms, bureaux de change and pawnshops.

32. The money laundering offence is solidly based and applies to almost all acts, but the provision could be strengthened. It should be extended to allow persons to be prosecuted for laundering the proceeds of predicate offences which they have committed, and should allow for negligent money laundering in the same way as the offence of receiving. Most importantly, the suggestion that was made in the first mutual evaluation report that attempted money laundering be criminalised should be followed through. The provisions on confiscation and provisional measures are basically sound, and the tracing groups have achieved considerable success in depriving criminals of their proceeds. The system would be further strengthened if a governmental working group on the issue proposes provisions to reverse the burden of proof, and to tighten the law with respect to assets belonging to third parties which may be subject to confiscation. The Finnish system of laws and treaties concerning international co-operation provide an excellent model for other countries, and are very comprehensive apart from the need for some minor amendments regarding assistance in confiscation and provisional measures.

33. The Act provides a reasonably comprehensive and centralised base upon which to combat money laundering in the financial sector, and it makes the progressive move of extending the obligations to certain categories of non-financial businesses. The most important weakness that remains is to bring all forms of the money remittance/transfer business under the scope of the Act, and to make this business and the bureaux de change subject to supervision by the FSA. Legislative measures concerning the financial sector meet the FATF Recommendations, and appear to have been effectively implemented, at least in the banking sector, with the FSA playing an active role. Despite this, it is a matter of concern that the number of STR up until 1997 remained very modest, that there has been a continuous decline in the number of reports made since 1994, and that the reports have been received mostly from several large banks, with few reports received from the insurance sector, bureaux de change, and securities firms. Based on the available evidence, it seems that the number of reports is unlikely to increase unless there is an increased effort from the MLCH, the FSA and other authorities with respect both to education and training, and to further develop a fully co-operative partnership with the reporting institutions.

34. The changes that have recently been implemented in the Act, and the creation of the MLCH means that it is too early to fully assess how effective these measures will be, but the new administrative arrangements mean that the MLCH will be a focal point for anti-money laundering activity in Finland, and will be able to build upon the efforts that have been made so far. It has access to a wide range of information sources, and sufficient resources to properly investigate and analyse the reports, provide feedback, and arrange and participate in training and education of the financial and non-financial sectors which are covered by the Act and also the local police forces. Its active participation in such activities is necessary for the system to progress further. It is already an active participant in international co-operation, and its new role as the central FIU will enhance that.

35. Overall, the anti-money laundering system in Finland now meets almost all of the requirements of the FATF Forty Recommendations, and in certain areas, such as mutual legal assistance, it has enacted legislation which has the potential to be very effective. The government has followed most of the suggestions for improvement in the first mutual evaluation report, which has enhanced the system and created a firmly based legislative and administrative structure. However, results in a number of areas are quite modest, and concentrated efforts will be required to revitalise the reporting of suspicious transactions, though the new system is at an early stage of development and improvements are still being made. Though several further legislative and administrative measures are required, a platform has been built which, with some refinements, will provide a sound springboard for the future.

Luxembourg

36. Types of criminal activity giving rise to laundering in Luxembourg include drug trafficking, organised crime and financial crime. As for other important financial centres, it can be reckoned that nearly all the big traditional crime organisations are also represented in Luxembourg, being attracted by its international commercial and financial infrastructure.

37. In compliance with the FATF's Forty Recommendations, Luxembourg set up an anti-money laundering mechanism comprising preventive measures and penal sanctions. The preventive measures were introduced under the Act of 5 April 1993 related to the financial sector. They apply to banks and other financial businesses. The Act of 18 December 1993 on the insurance sector extended the same provisions to life insurance companies. The measures concerned aim primarily at prevention of laundering and introduce an obligation for businesses subject to the disclosure requirement to co-operate in the matter of detecting suspicious transactions and reporting them to the Public Prosecutor's Office.

38. The penal sanctions were introduced under the Act of 7 July 1989 supplementing Luxembourg legislation on sales of medicinal substances and control of drug abuse, and under the Act of 17 March 1992 approving the United Nations Convention Against Illicit Traffic in Narcotic Drugs and Psychotropic Substances and adding, *inter alia*, the principle of confiscation of the proceeds from offences and of the revenues derived from impounded goods. With the Act of 11 August 1998, introducing the offences of organised crime and money laundering into the Penal Code, a response has been given to FATF Recommendation 4. The Penal Code will contain a new section dealing specifically with the offence of money laundering.

39. Having regard to the new FATF Recommendations 8 and 9, the Act of 11 August 1998 supplements the expanded definition of the laundering offence with an extension of the laundering prevention and detection system to certain professions and businesses most liable to be involved in laundering operations or confronted with them. Thus the reporting requirement is extended to notaries, casinos and games of chance establishments, and company auditors, and the requirement to identify the beneficial owner is extended to notaries.

40. Although the legal framework of Luxembourg's anti-money laundering system broadly conforms to the FATF Recommendations, its actual effectiveness is still difficult to assess. The low number of suspicious activity reports raises a good many questions. In fact, the functioning of the Luxembourg anti-money laundering system could be better assured, and could better preserve its reputation as a financial centre where the assets held by non-residents are very considerable, if it more actively used all the possibilities offered by its legal framework, notably in terms of reporting of suspicious transactions and of checking of the effectiveness of anti-money laundering measures.

41. As regards disclosure of suspicions, it is almost always the same banks that report suspect transactions. A large number of financial institutions have never made a disclosure. Without seeking to

change the essentially preventive nature of the system applicable to financial institutions, it seems absolutely essential to establish a broader conception of reporting requirements that would make it possible to deal with information on the large number of customers who are refused by banks, in particular, on grounds of suspicion and who cannot be linked to specific criminal offences.

42. Therefore, the Anti-Money Laundering Service should also be strengthened so as to be able to meet an increase in the number of suspicious activity reports and maintain a cross-disciplinary capacity. Indeed, the staff of the Anti-Money Laundering Service of the Public Prosecutor's Office should be completed by financial experts in order to perform its tasks of analysing and expanding case files. It could thus deepen the work of investigating transactions and improve its knowledge of the financial sector, possibly with the collaboration of the IML. The expertise of the latter in this area would allow it to draw general conclusions regarding its preventive role on the basis of investigations it should undertake on concrete deficiencies.

43. There should probably also be tighter monitoring of the reporting practices of financial institutions. This would be facilitated by closer co-ordination between the supervisory authorities and the law enforcement services so as to make it possible to target the most serious defaults, give instructions to professionals accordingly and perform on-site checks of compliance. The exemplary value of formal procedures of sanctions should be duly acknowledged, whether they are penal or administrative.

44. Since the first evaluation, the authorities have concentrated their efforts on implementing the system introduced in 1993. In 1997, several important bills of law were put before Parliament. The measures contained in the Act of 11 August 1998 -- such as enlargement of the scope of the money laundering offence and extension of the preventive legislation to non-financial professions and those which are still at the stage of draft, such as the introduction of new rules for company domiciliation agents, and reform of the judicial procedure for mutual assistance -- should provide the competent authorities with additional legal means to be effective in detecting and punishing money laundering.

Ireland

45. Drug trafficking crimes are considered to be the major source of significant illegal proceeds laundered in Ireland, with much of it controlled by criminal gangs. Since the first FATF evaluation, there has been a significant increase in the amount of drug trafficking in Ireland, as well as an increase in the organised nature of the criminal activity. Other offences which generate significant proceeds are fraud and other economic crimes, smuggling of cigarettes and alcohol, and terrorism. The principal money laundering methods and trends which have emerged include: the use of other persons accounts by the principal offender; the deposit of monies in accounts in other countries; the exchange of criminal proceeds into foreign currencies; the purchase and development of properties or high value items; early encashment of insurance products, preferably single premium insurance policies; and the use of established businesses, particularly those which are cash based such as pubs, shops, garages and bookmakers. Although Ireland is not a major money laundering centre, there has been a marked increase in the amount and variety of methods by which criminal proceeds have been laundered.

46. The policy and objective of the Irish government is to combat money laundering particularly in the context of the fight against organised crime and drug trafficking. Since the date of the first evaluation visit, the entire Irish anti-money laundering system has been put in place. The most significant change was the enactment of the Criminal Justice Act 1994 (CJA) which introduced provisions creating an all crime money laundering offence, confiscation provisions and provisions concerning the financial sector such as the mandatory reporting of suspicious transactions, customer identification and record keeping. The Act also contains provisions providing for mutual legal assistance. In 1995, a Money Laundering Investigation Unit (MLIU) was established within the police to receive, analyse and investigate

suspicious transaction reports. In 1996 Ireland ratified and fully implemented the 1988 Vienna Convention, and the 1959 and 1990 Council of Europe Conventions. The enactment of the Proceeds of Crime Act 1996 (POCA) allowed for the seizure and civil forfeiture of property which is the proceeds of crime, and this is enforced by a new multi-agency body - the Criminal Assets Bureau (CAB). It has also been recently decided to extend the financial sector requirements of the CJA to accountants, auctioneers and estate agents, and solicitors, and consideration is being given to including company formation agents.

47. The money laundering offence is satisfactory though the number of convictions to date is quite low, and this could be enhanced by removing the requirement to prove that the acts took place for a particular purpose, and casting the mental element of the offence more broadly. The powers to freeze and confiscate property are very wide-reaching, and the POCA is being aggressively and successfully implemented. If the assumptions in the CJA were widened to all criminal offences, and there was increased focus on the CJA this may also reap similar benefits. With respect to cross border controls, the extension of the cross-border seizure and forfeiture provisions to all serious crime, and to go beyond cash to cover other financial instruments, would lead to a more comprehensive and consistent system. The Irish system of laws and treaties concerning international co-operation are comprehensive and though it is too early to tell how effective they will be, the system of formal mutual legal assistance seems to be working successfully so far. With respect to informal operational assistance there are no impediments to exchange of information between the MLIU and other FIU, though there is an over-strong reliance on informal discussions or contacts, which should be rectified by entering into formal memoranda of understanding, particularly with administrative FIU.

48. The law enforcement response to money laundering and the proceeds of crime has centred around the MLIU and the CAB. The MLIU has experienced a steady increase in the number of reports received, and has concentrated on investigating these reports, and this factor, together with the lack of a financial analyst may prevent it from carrying out a full range of operational, tactical and strategic analysis work. Staffing is inadequate to properly perform both the full intelligence function of an FIU and to investigate cases through to prosecution, and there needs to be a clear demarcation between the intelligence function and the investigative function. The CAB is a multi-agency body with a range of expertise to draw upon and extensive legislative powers, which it has utilised to full effect. In addition, the ability of the CAB to use a variety of other civil recovery tools has proven to be very effective, and the government should consider whether some of the successful components of this system could be used in other areas of law enforcement. The system could be further strengthened by the creation of more information gateways, a stronger exchange of information and greater co-operation between all agencies involved in combating crime, including the Customs and Revenue authorities.

49. The legislative measures dealing with customer identification, record keeping, and reporting of suspicious transactions meet the FATF Recommendations, and when combined with the sets of guidance notes provide a comprehensive base upon which to combat money laundering in the financial sector. In most respects the anti-money laundering system has also been reasonably effectively implemented, and when the various categories of non-financial professions are made subject to the obligations in the CJA it will have a broad scope, though money remittance business should also be brought under the CJA. The Central Bank and the Garda Síochána (Irish Police) need to consider how to deal with a limited number of unauthorised and thus unsupervised bureaux de change, and attention also needs to be given to the scope of the exemption requirements relating to customer identification, and as to how the level of feedback can be improved in an efficient way. Another important concern with respect to reporting, as in many other countries, is the low level of reports from outside the banking sector, and this should be the focus of attention. The Central Bank has taken an active approach regarding the credit institutions and financial institutions which it supervises, and internal controls, guidelines and training are generally very satisfactory. However, increased supervisory attention needs to be paid to the insurance sector and given

that almost all NBFI are regulated by the Central Bank it would appear logical and beneficial that the function of supervision of insurance companies be transferred to the Bank.

50. Since the first evaluation visit, Ireland has put in place a comprehensive and very solid legislative scheme for combating money laundering, which meets almost all the FATF Recommendations. In relation to certain measures, such as the POCA and the CAB, it has implemented an innovative legislative and administrative scheme, which could provide a model for other countries. These measures, together with an active implementation in important areas such as Central Bank supervision, and a willingness to review the system and make appropriate changes, provide a firm foundation for an effective anti-money laundering system.

Hong Kong, China

51. Trafficking in dangerous drugs is assessed to be the criminal activity which generates the most criminal proceeds in Hong Kong, China. Traditionally drug trafficking in Hong Kong has taken two forms, namely, supply for the domestic market, and transhipment to other international markets. In addition to drug trafficking, loan sharking, gambling (both illegal casino and bookmaking) and economic crimes are considered to be major sources of illegal proceeds. Hong Kong continues to be a major international financial centre which is free and open. The financial system is characterised by a low tax system, sophisticated banking facilities and the absence of currency and exchange controls. Like other international financial centres sharing these characteristics, Hong Kong is susceptible to money laundering activities.

52. Over the years, Hong Kong has developed legal and financial systems to counter money laundering. Hong Kong enacted its first drugs-related money laundering legislation in December 1989. Since then, both the Hong Kong Police Force and the Customs and Excise Department have been empowered to investigate drug money laundering cases. A Joint Financial Intelligence Unit (JFIU) of both departments has been established to facilitate the reporting of suspicious money laundering activities and to co-ordinate the investigation of these suspicious activities when warranted.

53. Other than the legislative measures, financial service regulators have updated their guidelines on money laundering and issued these guidelines to the industries of which the regulators respectively exercise prudential supervision. These guidelines require the industries to observe the standards and procedures in record-keeping, customer identification and reporting of suspicious transactions.

54. Since the first evaluation in 1994, Hong Kong has taken a number of important steps in its anti-money laundering regime. The expansion of its anti-money laundering legislation under both the Drug Trafficking (Recovery of Proceeds) Ordinance (DTRoP) and the Organised and Serious Crimes Ordinance (OSCO), which include the extension of the money laundering offence from only drug trafficking to the proceeds of serious crimes and statutory mandatory suspicious reporting, have provided a solid foundation for penal action. The money laundering offences and new confiscation legislation appear to be fundamentally sound, though a low number of convictions are a matter of concern.

55. Since Hong Kong has made the reporting of suspicious transactions mandatory for both drug offences and other serious crime, there has been a substantial rise in the number of suspicious transactions reported from 1995 onwards. Despite these accomplishments, and the efforts to raise awareness of the potential money laundering problem, extensive non-compliance with suspicious transaction reporting requirements continues to exist among unregulated remittance agencies. In addition, the number of reports received are still small, relative to the size of the Hong Kong financial markets and reporting levels in other jurisdictions. It should be noted that the vast majority of reports are made by a few of the larger banks with few, if any, reports being made by insurers, insurance agents,

accountants, solicitors and securities participants. The insurance and the securities regulators should therefore increase the emphasis they place on anti-money laundering systems and encourage their constituents to report suspect activity.

56. While this is not unique to Hong Kong, the ready availability of shell corporations continues to hamper the anti-money laundering regime. In order to strengthen its anti-money laundering regime, Hong Kong will have to regulate this sector more effectively. While the Hong Kong Police is to be congratulated on their proactive work in relation to money changers and remittance agents (anti-money laundering guidelines, extensive programme of educational visits), there is still a need to regulate formally these groups which remain as loopholes in the anti-money laundering system.

57. As a whole, commendable efforts have been made by Hong Kong authorities to improve the deficiencies identified in the first mutual evaluation. However, the low number of suspicious transactions reports and of convictions for money laundering, suggests that the effectiveness of the system can be further improved. It is expected that the enactment and implementation of the various measures under consideration (standard of proof, coverage of bureaux de change and remittance businesses) and greater efforts by regulatory authorities will result in a more effective anti-money laundering system.

New Zealand

58. The money laundering activity detected in New Zealand seems largely domestic in nature and is deemed by the authorities to be relatively small when considered in the international context. The main source of illegal proceeds can be categorised into three offences: drug; fraud and other offences against property, including theft, burglary and receiving stolen goods. The offences which generate the most money involve drugs followed by fraud and then other offences involving dishonesty. These offences tend to be the main focus of Police efforts in identifying criminal proceeds.

59. The New Zealand authorities report that there is no evidence to suggest that any domestic banks or non-bank financial institutions have been significantly penetrated by foreign drug cartels. However, New Zealand may be considered to be an attractive target country for money laundering because it is politically stable, has a developed economy and a sophisticated financial sector. There is also some evidence that New Zealand is used as a transit country for drugs and also for illicit money coming from Central and Eastern Europe countries which is then wire transferred to the offshore financial centres of the Pacific. In addition, Customs drug investigations have shown an increase in the activities of organised crime groups in New Zealand and some unusual or unexplained movements of cash. However, the frequency and size of these activities seem to be relatively modest.

60. Since the first evaluation in 1994, New Zealand has significantly improved its compliance with the forty Recommendations with the introduction of a money laundering offence (amendment to the Crimes Act), the enactment of the Financial Transactions Reporting Act (FTRA) and the 1998 amendments to the Misuse of Drugs Act and the Mutual Assistance in Criminal Matters Act. These pieces of legislation provide a solid foundation for repressing, detecting and preventing money laundering in New Zealand. In addition, some small fine tuning amendments are already underway. Reviews of both the Proceeds of Crimes Act 1991 and the reporting regime at the border are planned within the next year. The Government is also committed to participation in international initiatives against money laundering, particularly at a regional level.

61. Guidance Notes for financial institutions have also been circulated. Furthermore, the New Zealand authorities have promoted the awareness of anti-money laundering laws among financial institutions and customers of banks. It should be noted that these efforts have been made with very limited resources.

62. Although the legal framework is in place and the New Zealand authorities have promoted the awareness of money laundering, they prefer a different approach to the question of compliance, relying on market and general incentives, rather than ensuring that there is strict adherence to laws and guidelines. Generally, the approach of the New Zealand authorities is that New Zealand has adopted measures it considers appropriate to its circumstances and has faith in financial institutions regulating themselves, as these financial institutions have their own interests and reputation to protect as exposure to large scale money laundering is a business risk. Some regulators appeared not to be at all involved in the anti-money laundering strategy because they rely on the institutional framework. In addition, there appears to be varying degrees of anti-money laundering efforts undertaken by the banks on the one hand and by the non bank financial institutions and the non-financial businesses on the other. A wider permeation by regulators has proved in other jurisdictions to provide a greater appreciation of anti-money laundering initiatives to the financial institutions.

63. One cause of concern is the fact that some financial institutions do not need to register with the Reserve Bank or any other supervisory authority. It seems that, although understanding that the Government of New Zealand does not wish to impose excessive compliance costs on the private sector, some closer scrutiny of the financial institutions by the supervisory public authorities could enhance the effectiveness of the system.

64. New Zealand's anti-money laundering system, which addresses virtually all the areas covered in the forty Recommendations, has only been in effect since August 1996, and it might therefore be too early to draw firm conclusions on its impact on money laundering. Available statistics do not permit a comprehensive assessment of the effectiveness of this recent system. It is nevertheless expected that the legislative changes recently adopted (the amendments to the Mutual Assistance in Criminal Matters Act) or being considered (Extradition Bill) or being reviewed by the Government (Proceeds of Crime Act, Cash Border regime) will improve the counter-measures. In addition, changes concerning the standard of knowledge, confiscation and provisional measures, together with closer scrutiny of the compliance of financial institutions with the anti-money laundering requirements, could result in a more effective system.

Iceland

65. Iceland is a geographically isolated country with a small population, and a financial sector which does not presently have many links with other countries. It does not appear to be a prime money laundering target nor does it presently have a significant laundering problem. As in 1994, drug trafficking together with various kinds of economic crimes remain the most significant sources of illegal proceeds in Iceland. The incidence of fraud and economic crimes, particularly crime related to customs and tax fraud, have doubled since the first evaluation, and these offences are also now among the most common crimes in Iceland. Smuggling of tobacco and alcohol is most common, though importing cars with false invoices has also occurred quite frequently, and almost all the smuggling activity is linked to organised crime. However, in general, it is not thought by the authorities that these financial crimes give rise to any significant money laundering. Drug trafficking and related crimes are however increasing, and though the Icelandic authorities have knowledge of only a few cases of money laundering, these primarily related to drug trafficking. They also observed that the majority of suspicious transaction reports (STR) concerned the purchase of foreign currency, and cross border transportation of cash.

66. The Icelandic policy on money laundering is to ensure that Icelandic legislation is aligned with the FATF forty Recommendations, and to increase awareness of the potential risks of money laundering for all financial or non-financial institutions in Iceland. Emphasis is also placed on ensuring that sufficient resources are available to deal with the reports of suspicious transactions and to investigate money laundering offences. Since the first evaluation, the most significant amendments have been the

ratification in 1997 of the Vienna and Strasbourg Conventions, and the amendment of the Penal Code to extend the money laundering offence to the proceeds of all crimes contained in that Code, including major tax crimes. Money laundering was also made a separate criminal offence under the Penal Code. In 1998, the government also introduced a Bill into Parliament which will, inter alia, extend the application of the Measures Against Money Laundering Act to all institutions or persons which engage in one or more financial activities (as listed in the Forty Recommendations), as well as to gambling operations.

67. Iceland has modified its domestic legislation in important ways since the last mutual evaluation, and emphasis must now be placed on effective implementation. The money laundering offence now applies to a wide range of predicate crimes, but some refinements could make it even more effective. Thus consideration could be given to widening the *actus reus* of the offence, and to the sentencing powers which are held by the court. Confiscation is treated as a low priority issue and the results obtained to date are minimal. Iceland should review the provisions concerning confiscation, provisional measures and related powers of investigation, and implement changes where appropriate, including any necessary changes to law enforcement structures. As regards mutual legal assistance mechanisms, they appear to have a broad application, and allow for a wide range of assistance, though experience is very limited to date.

68. The unit for serious tax and economic offences at the National Commissioner for Police is playing an increasingly important role in the Icelandic anti-money laundering system. In addition to investigating economic crime, it acts as the FIU and receives the STR for analysis and investigation. So far results have been very limited, and the Unit has managed with limited resources, however if it is to fully develop the functions of an FIU, it will need increased resources. This will allow it to perform tasks such as proactive analysis and targeting, international co-operation, providing increased training and education for the financial sector and for local police forces, as well as giving increased feedback. Efforts should also be made to co-ordinate and co-operate with the Customs authorities more closely in appropriate areas.

69. As noted above, though the Money Laundering Act presently has a limited scope, the new Bill will substantially widen this to cover a wide range of businesses, including bureaux de change, money remittance businesses and professionals such as lawyers or accountants, when engaging in financial activities on behalf of their customers. This widening of the Act is to be welcomed, though appropriate supervision measures will need to be implemented. The legislative measures dealing with customer identification, record keeping, reporting of suspicious transactions, internal controls and supervision all substantially meet the FATF Recommendations, and the obligation on reporting institutions to examine and report on unusual or complicated financial transactions is a desirable extension of the normal requirements. Despite this, it is matter of concern that the number of STR has remained very modest and the results are unevenly distributed. Moreover, further steps need to be taken to ensure a comprehensive and consistent set of guidance notes for financial institutions.

70. Generally, the anti-money laundering system in Iceland is solidly based and meets most of the essential requirements of the FATF Forty Recommendations. The government has responded positively to some of the suggestions for improvement in the first mutual evaluation report, and this, together with the Bill introduced in 1998, will lead to an enhancement of the system. Some further refinement of the legislation still needs to take place, but in many areas, practical experience with the suspicious transaction reporting system and money laundering cases is required before a proper assessment can be made as to whether the system is working effectively.

Singapore

71. Singapore regards drug trafficking as the criminal activity which generates the major component of illegal proceeds in the jurisdiction, though the majority of drugs seized in Singapore are in

transit to other countries. Though several examples of economic crimes involving large amounts of money were available, there has been a fall in the number of crimes since 1994, and it is not clear if such crimes are regarded as a serious problem. Similarly, little information was available on the extent to which the proceeds of foreign drug trafficking and other serious offences are laundered through Singapore, or on the money laundering techniques and methods that are most prevalent in Singapore. However, given the limited market for illegal drugs in Singapore and the strong penal regime, it is likely that money laundering activities in Singapore will principally involve the proceeds of domestic and foreign commercial offences, and foreign drug trafficking offences. In addition, Singapore is an important, modern and competitive financial centre in Asia with many local and foreign financial institutions and a sophisticated and reputable banking structure, and these factors may make it susceptible to persons who wish to launder the proceeds of foreign offences.

72. Singaporean anti-money laundering policies are based on strong anti-drug policies, combined with strict selection criteria for banks and financial institutions seeking admission to their financial sector and strict financial supervision. Few legislative amendments have been made since the first evaluation, though Singapore did accede to the Vienna Convention in October 1997, and amendments in June 1998 made drug money laundering an extraditable offence under the Extradition Act. The anti-money laundering guidelines have been extended to insurance companies, bureaux de change (money changers) and money remittance companies. A draft Bill has also been prepared which will amend the Drug Trafficking (Confiscation of Benefits) Act, so as to replicate almost all the current provisions applicable for drug trafficking and apply them to a wide range of serious offences. The main changes that are being proposed are: (a) to criminalise the laundering of the proceeds of a wide range of serious offences; (b) to facilitate the prosecution of money laundering offences by allowing the prosecution to rely on the lower standard of "reasonable grounds to believe"; (c) to impose a requirement on all persons to report transactions if they have reasonable grounds to believe it involves the proceeds of a serious offence; and (d) to extend the powers of confiscation and provisional measures to the list of serious offences.

73. Since the first evaluation only a few amendments have been made to the anti-money laundering system, and few of the proposals contained in the first mutual evaluation report have been introduced. Although a lack of data in some areas made assessment more difficult, it is clear that despite some strong features there are significant weaknesses in relation to the legislative, financial counter-measures and procedural aspects of law enforcement which exist in Singapore, that Singapore is out of compliance with a number of FATF Recommendations, and that the results of the system could be considerably improved. An urgent review of the entire system is required, but efforts should be concentrated on ensuring that: (a) all the relevant measures apply not only to drugs but to a range of other serious crimes; (b) clear and comprehensive mutual legal assistance legislation is enacted, combined with a range of treaties; and (c) the legal and administrative system for suspicious transaction reporting is significantly more efficient and effective.

74. The proposals to extend the money laundering offences in the draft Bill to a wide range of serious offences, as well as reducing the *mens rea* to the level of "reasonable grounds to believe", show a desirable intention to make the provisions more effective, and improve on the current lack of results. However the current proposals appear to be unduly complicated and may lead to unnecessary difficulties in implementation, and it is proposed that a review be conducted of the legislative developments that have taken place elsewhere before proceeding to enact new legislation concerning the offence, confiscation provisions and investigative powers. Consideration needs to be given to extending any new money laundering offence to all indictable offences, and to widening the basis for reporting to the level of suspicion, whilst some technical amendments could also make the offence more effective. The confiscation laws, which are fundamentally sound, also have the capacity to be more effective, and the widening of their application to a wide range of crimes will undoubtedly assist in this. However, results

to date are modest, and could be improved by a number of technical amendments, as well as by a consideration of legislative measures being adopted in other countries with similar legislation.

75. Law enforcement powers of investigation are adequate and appropriate for domestic investigations, but due to bank secrecy and the pre-requisites for obtaining court orders, the law enforcement agencies are unable in practice to use these powers to obtain information from financial institutions so as to assist other countries in international cases. This should be reviewed in the context of the introduction of mutual legal assistance legislation. The law enforcement agencies which deal with money laundering and confiscation, are motivated and professional in their approach. Under the proposed extension of coverage to serious offences, the division of responsibilities needs to be reassessed to ensure there is no duplication of effort. The very low number of suspicious transaction reports, the lack of results, and the need for increased emphasis on proactive financial intelligence and investigation shows that it is essential that a dedicated FIU be created to deal with all aspects of the suspicious transaction reporting system. This needs to be linked with a multi-disciplinary body with expertise from several agencies, which could handle the range of tasks which are necessary if effective measures are to be taken against money laundering and the proceeds of crime. This could be complemented by an increase in the level of co-ordination and co-operation, both at a law enforcement level and across government.

76. In the financial sector, the Monetary Authority of Singapore's (MAS) Guidelines lay out the fundamental requirements, but significant elements of the Guidelines effective at the time of the evaluation were often vague, imprecise, and not adapted to the needs of the different types of financial institutions. This should be rectified by introducing binding requirements which lay out obligations, and provide assistance on practical issues or points of detail. In this connection the first positive steps were made by updating the guidelines in January 1999. Clear requirements need to be introduced under Recommendation 11, obligating financial institutions to identify the beneficial owner of an account or transaction. The current provisions dealing with reporting of suspicious transactions are confusing and contradictory. Singapore must urgently introduce a single section which requires persons and companies to report suspicions that a transaction or attempted transaction involves property which is the proceeds of, or instrumentality of, serious criminality. Ancillary provisions must also be introduced, such as sanctions for failure to comply with the reporting obligation, full protection from liability if a report is made in a bona fide and timely way, and a more effective tipping-off offence. The lack of feedback is almost certainly a contributing factor to the low level of reports, and action must be taken to provide a full range of general and specific feedback, which could be linked to increased co-operation with the financial sector through regular meetings.

77. Supervision is generally very tight, with the MAS having considerable persuasive powers to ensure that the financial community comply with the appropriate standards. Despite this, the obligations relating to internal controls need to be expanded in order to comply fully with Recommendations 19 and 20, and the Guidelines need to be updated and, where necessary, different requirements imposed for different types of financial institutions. There should also be increased emphasis on training, with greater involvement by government agencies. Consideration also needs to be given to the withdrawal of the S$10,000 note, and the introduction of appropriate measures at the border which would introduce a system of declaration and monitoring, and/or seizure and forfeiture of criminal proceeds.

78. International co-operation is the area where the most significant advances have been made since the last evaluation, but it also contains some of the major deficiencies that still need to be rectified. The accession to the Vienna Convention and the making of drug money laundering an extraditable offence were important advances, however the lack of mutual legal assistance legislation, the failure to have entered into any mutual legal assistance treaties, and the inability to co-operate effectively in relation to STR create significant difficulties for rendering assistance to foreign authorities. These shortcomings

have, on occasions, been exploited by foreign drug traffickers and other foreigners committing serious criminal offences.

Portugal

79. Drug trafficking is considered to be the main source of money laundering in Portugal. The country's geopolitical situation -- facing the south Atlantic with a very long seaboard, close to north Africa and with cultural and linguistic ties with Africa and South America -- explains why Portugal is one of the entry points in Europe for international trafficking in narcotics and psychotropic substances. Money laundering does not seem be on a significant scale. Among the most common methods used were electronic fund transfers sent by companies in offshore centres to bank accounts also in such centres, and the channelling of money through bureaux de change.

80. Since 1993, the Portuguese legal system has been brought into line with international agreements on money laundering by the approval of Decree-Law No. 15/93, the publication of Decree-Law No. 313/93, which transposed EEC Directive 91/308 into Portuguese law, and more recently, by the coming into force of Decree-Law 325/95, modified by Law 65/98 of 2 September 1998, which increased the number of money laundering predicate offences and introduced measures of control to non-financial institutions. Portugal also ratified the 1990 Council of Europe Convention on laundering, search, seizure and confiscation of the proceeds of crime.

81. Following this legislative phase consisting of the adoption of specific measures to prevent the laundering of money from drugs and other types of crimes, anti-money laundering policy has entered a new phase. It aims to incorporate the provisions of the Strasbourg Convention into the Portuguese legal system and to remedy certain shortcomings in order to facilitate international judicial co-operation on criminal matters, as provided by Decree-Law No 43/91 of 22 January 1991.

82. The new government initiatives to combat money laundering are at two levels:

- firstly, at the domestic level, by training officials to combat money laundering and to use new technologies so as to facilitate investigations;
- secondly, at the external level, via bilateral and multilateral co-operation in the legal and police area, in particular with EU countries, Portuguese-speaking African countries, Brazil and other countries.

83. Following the legislative changes in 1995, the Portuguese anti-money laundering system is one of the widest in scope, as regards both the types of criminal behaviour and the financial and non-financial businesses covered. This illustrates the political commitment of the Portuguese authorities to combat coherently the money laundering phenomenon, and as a pioneer in some areas.

84. Although the Portuguese system complies with FATF Recommendations, its real effectiveness is difficult to determine. There is evidence of a real political determination to combat money laundering but the practical results have been rather meagre, especially in terms of the number of suspicious transaction reports. This also applies to the amount of funds finally confiscated under court judgements compared to provisional seizures of assets and funds.

85. The legal machinery is sufficiently comprehensive, though there is a need for harmonisation between drug trafficking and other primary offences with regard to both criminal conspiracy and money laundering. The same applies to confiscation rules, which differ according to whether a prosecution is brought for money laundering linked to drug trafficking or money laundering linked to other offences. The practical effectiveness of the system of confiscation independent of conviction is difficult to evaluate because there is no case law in the matter.

86. The financial sector as a whole plays a decisive part in prevention, in particular through strict and comprehensive customer identification measures. It is possible, however, that the informal approach to implementing the system for reporting suspicious transactions may undermine the effectiveness of detection. Some players in the financial sector, especially insurance companies and exchange bureaux, and the entire non-financial sector currently make no more than a marginal contribution to the system for reporting suspicious transactions. Intensive awareness and training initiatives in these sectors would do much to improve this situation.

87. On the law enforcement side, the active element of Portugal's anti-money laundering machinery is a special brigade of the Judicial Police, the BIB, within the anti-drug trafficking department. This unit, which is unlike structures in other countries, functions in practice as a national centre for gathering and processing financial intelligence, including both police investigation and criminal proceedings. However, progress could be made towards greater clarification of the role of each unit involved in the processing of information. The fact that all information passes via the State Prosecutor's Office has a high symbolic value, but is perhaps no longer entirely necessary in view of the increasingly important role played by the DCIAP.

88. Banking and financial specialists could usefully be added to the BIB's strength on a permanent basis. As well as helping police officials in their investigations they could establish and maintain contacts and informal dialogue with reporting entities with a view to obtaining additional information. Likewise, a structure within the BIB or DCIAP, albeit a lightweight one, to manage relations with outside correspondents, whether Portuguese or foreign, would both help to ensure continuity and free up analytical or investigative staff for operational tasks.

89. Lastly, it is striking to see that many activities that could be channels for money laundering, such as gaming, property and jewellery, are strictly regulated and controlled by the authorities. It would be instructive to seek confirmation over time that existing measures are reasonably effective.

90. The Portuguese authorities have worked very hard to establish a particularly comprehensive anti-money laundering system. All players, in both the public and the private sector, have mobilised their forces to implement wide-ranging prevention measures. Greater co-operation between the parties concerned and better feedback would probably help to improve the system's operational aspects. In particular, the flow of suspicious transaction reports needs to be stepped up further.

Turkey

91. Since the first evaluation Turkey has introduced a considerable number of new measures, the most important being the enactment in 1996 of Law No. 4208 on the Prevention of Money Laundering (the Money Laundering Law), which introduced a money laundering offence based on a range of predicate crimes and other ancillary provisions. Subsequent regulations and decrees have required banks, non-bank financial institutions and some non-financial businesses to identify customers for transactions in excess of 2 billion Turkish Lira (USD 6,600), keep records, report suspicious transactions, and provide some guidance on these issues. Turkey also ratified the Vienna Convention in November 1995, and established the Financial Crimes Investigation Board (FCIB), which will act as the Turkish financial intelligence unit (FIU). Despite these significant advances, some further measures are required.

92. Drug trafficking remains the single largest source of illegal proceeds in Turkey, with the level of drug consumption in Turkey increasing since the first evaluation. According to the Turkish authorities, organised crime groups traffic a significant amount of the narcotic substances smuggled into Turkey by way of the southern and south-eastern borders. After drugs, the crimes which generate the greatest amounts of illicit proceeds are use of falsified invoices, smuggling of weapons and explosive materials, smuggling of historical works and smuggling of items of cultural or natural importance. Generally, it

appears that there have been an increasing number of both drug cases and financial crime cases in recent years. On the limited information available, it is apparent that the most common money laundering methods used are smuggling money across borders using couriers, bank transfers of funds into or out of the country, and investments in high-value real estate, luxury automobiles and other vehicles, and in gold and other precious metals. It is also believed that there is a link between money laundering and the groups involved in organised crime.

93. The legal provisions provide the basic measures which are required, and the money laundering offence extends to a broad range of predicate offences. Despite this, requiring that the prosecution prove knowledge or intention will impose a substantial burden on them in money laundering cases, and it would be desirable if an alternative lower standard was also introduced, perhaps with lower penalties attached. A set of basic provisions concerning confiscation and provisional measures is included in the Criminal Code, with some additional measures in the Money Laundering Law, but a lack of statistics prevented an accurate determination of the effectiveness of these provisions. Certain requirements such as the need for the prosecution to prove to the criminal standard that property is the proceeds of the crime of which the person has been convicted will make these laws less effective. The government should review the laws and measures that exist in this area, compare them to modern developments in other countries, and implement the necessary changes. Measures regarding international co-operation by the FCIB appear to be generally adequate, though the need for a mutual legal assistance treaty, once a case has been passed to a prosecutor, may be a limiting factor. In addition, it is not clear whether there are any other obstacles to co-operation, but if so, they should be reviewed with the objective of achieving more effective and efficient co-operation. Turkey should also move expeditiously to seek to accede to the 1990 Strasbourg Convention.

94. The Money Laundering Law introduced mandatory suspicious transaction reporting, and together with the amendments to the Banking Act in April 1998 substantially satisfies the customer identification requirements. The need to identify the beneficial owner should be extended to apply to all persons, real and legal, and the lack of obligation and of any sanction for banks and other liable institutions should be amended. The provisions that apply for reporting of suspicious transactions are generally satisfactory, but the low level of results (20 suspicious transaction reports in the first 10 months of 1998) causes considerable concern, and a range of measures need to be undertaken to improve this situation. In particular, the government and the FCIB needs to improve their working level co-operation with financial institutions, and their support of the training which is carried out by the financial sector. Improved feedback and the introduction of an audit and compliance programme should also assist in increasing the results.

95. Turkey does not currently meet Recommendations 19 and 20. There are no internal control obligations, such as a requirement to have compliance officers, written policies, ongoing training etc., and legal obligations addressing these issues need to be urgently introduced for all parts of the financial sector. Similarly, there are no obligations imposed on financial institutions to ensure proper compliance with Recommendation 20, which is of concern due to the location of a number of branches or subsidiaries. These steps will need to be combined with a comprehensive set of guidance notes. Another important area of weakness is the lack of active supervision. A programme of off-site and on-site supervision of financial institutions is vital to the effectiveness of any anti-money laundering system, and the primary responsibility for this function should be taken on by the Treasury, the Central Bank and the CMB, which already supervise most of the financial sector institutions for general supervisory purposes. This supervision should commence as soon as possible, and the FCIB should operate to advise and support the mainstream regulators, though still retaining the capability of conducting on-site examination of particular institutions if it deems this necessary. Once this process is firmly in place, consideration should be given as to how to ensure adequate oversight and education of non-financial institutions.

96. The creation of the FCIB provided a focal point for Turkey's anti-money laundering effort, and the FCIB has the advantage of being well resourced, having a solid set of investigative powers, a willingness to act, and being a body with integrity, expertise and focus. Since it became fully operative in

1998, it has shown energy and commitment. However it cannot act alone, and the level of commitment and participation in combating money laundering and the proceeds of crime by all relevant government agencies needs to be increased. Secondly, a proper and effective mechanism must be introduced for co-ordinating this. The current Co-ordination Board is a useful first step, but the current structure of the body and its work programme are not appropriate for developing an effective action plan, either at the strategic or the operational level. Possible options for reorganising the Board include restricting membership to agencies that are integrally involved, having more frequent meetings during 1999-2000 at which fundamental issues can be determined, and having operational sub-groups to prepare detailed plans on specific issues. Critically important also is the need for a strategic plan to be developed that will address government objectives for the creation and implementation of an effective system in the medium term.

97. As part of a strategic reorganisation it is recommended that the FCIB review its present functions and divest the primary responsibility for money laundering supervision, but take on extra responsibilities as a lead agency in a more comprehensive approach to confiscation and the proceeds of crime. It also needs to more fully develop its FIU functions through strategic and tactical analysis, and by a closer and more co-operative relationship with the financial sector. In particular it will also need to develop strategies to increase the number of STRs. To achieve this, there is a need to widen the range of experienced staff. The FCIB should have a central role in increasing the level of co-operation and co-ordination at all levels – between law enforcement and operational bodies, across government, and with the financial sector. The financial sector needs to be actively involved and consulted on a regular basis on the government's anti-money laundering strategy if greater effectiveness is to be achieved.

98. Since the first evaluation Turkey has taken significant steps towards meeting the forty Recommendations and working to implement an effective anti-money laundering system. Despite these positive achievements, and the recent nature of many of these initiatives, the results in the first year have been moderate. Turkey should therefore continue to work to implement its system, but at the same time address and introduce the further steps identified above, so as to increase the effective of the system in the future.

Aruba (Kingdom of the Netherlands)

99. As in 1995, the most important criminal activity on Aruba stems from its role as a transit country for drug trafficking. According to law enforcement officials, there has also been a increase in the levels of drug consumption on Aruba, and of crime in general, and drug related crime accounts for 30-40% of crime on the island. Other predicate crimes on Aruba which appear to generate significant proceeds are fraud and tax fraud. The trend between money laundering and specified foreign predicate offences has not been clearly established, but the law enforcement authorities believe that laundering the proceeds of cocaine trafficking is significant. The authorities are uncertain of the money laundering techniques and methods that are most prevalent in Aruba, which makes it difficult to determine whether the amount of money being laundered has increased, and the degree to which the international payment system is being misused by money launderers in connection with the investment of illegitimate funds in Aruba or the layering of funds via accounts opened in Aruba.

100. Since the evaluation in 1995, Aruba has passed new legislation and undertaken a number of other measures aimed at strengthening its anti-money laundering system. In February 1996, the State Ordinance concerning the obligation to report unusual transactions in rendering financial services (the Reporting Ordinance), and the State Ordinance requiring identification when rendering financial services (the Identification Ordinance) came into effect. Following the passage of these measures, the Government has sought to address concerns relating to the casino and gambling industry, the use of legal entities, the import and export of cash and the Aruba Free Zone. Reports were prepared which make recommendations for strengthening the anti-money laundering measures in these sectors, and the necessary legislation has been drafted and is being discussed. These reports contain many valuable and innovative proposals, including improved licensing and supervision obligations, the

introduction of know your customer policies, and the implementation in the non-financial sector of other mechanisms to prevent money laundering, and will considerably strengthen the anti-money laundering regime, once implemented.

101. The penal provisions are generally broad in scope. The money laundering offence applies to all crimes, extends to cases where the defendant should reasonably have suspected that the money was from the proceeds of the crime, and has penalties that should provide a significant disincentive. However there are two major weaknesses. First, proof of the specific predicate offence underlying the money laundering is required, which may be very difficult in many cases. Second, the offences restrict the property which can be laundered to money, securities and claims, thus excluding real or other personal property, which will cut down on the effectiveness of the offences. The lack of prosecutions for money laundering since the offences were enacted in 1993 suggests these deficiencies may have had an effect. Changes need to be made to the legislation to make successful prosecutions possible. The legislation dealing with confiscation appears to be broad and potentially very effective, and the issue is the practical application of the legislation. New legislation has also been introduced to substantially increase the possibilities for international mutual legal assistance. In June 1999, the Vienna Convention was put into force, and the 1990 Council of Europe Convention is expected to enter into force on 8 July. Now that the legal framework is in place, Aruba will need further practical experience. At the level of informal co-operation, changes are needed to make it easier for the Reporting Center on Unusual Transactions (MOT) to exchange information with other FIU, and not requiring a formal treaty before this can take place.

102. The unusual transaction reporting system is a complex one, and the MOT has made significant advances since the system was implemented in 1996. However, adequate technical and human resources are needed to ensure that the system is working properly, and the system could be improved by increased qualified resources. Other measures which could make the system more efficient include: on-line access to police and public registers, electronic inputting of unusual transaction reports, and an ability to obtain information from the tax, customs and social security authorities. The police and prosecutors are pursuing some money laundering cases based on STR, but would benefit from use of more proactive financial investigation methods and increased training. It would also be desirable if the law enforcement/prosecutorial structure for enforcing the new confiscation laws is reviewed, and steps taken to encourage investigating officers and prosecutors to actively pursue confiscation as an integral part of a criminal investigation.

103. In the financial sector, the Identification and Reporting Ordinances, combined with the CBA Directive, have provided a very sound structural basis for anti-money laundering measures in the banking sector. However a comprehensive and consistent approach is required for both banks and NBFI, and certain financial services such as life insurance, money exchange or remittance, and pension fund activity should be put within the Identification Ordinance. The unusual transaction reporting system is working reasonably successfully so far, and the MOT and the ABA should be commended for moving to promptly review the system and to make the indicators more efficient. However, the total lack of reports from institutions other than banks needs to be promptly rectified, and the CBA should consider the circumstances under which it might report directly to the MOT. The MOT has worked to improve the level of feedback which is provided to financial and other reporting institutions, but further improvements could be made.

104. Internal control obligations and supervision for banks is mostly very sound, though the position of the two offshore banks is a matter of some concern. These institutions have no physical presence on Aruba, their records are kept in Venezuela, and they have made few unusual transaction reports. It is therefore recommended that the system that has been adopted to supervise these institutions be reviewed. A significant weakness is that neither the internal control requirements nor supervision extends to NBFI. The insurance sector will be covered when the new supervisory legislation comes into force, but measures need to be introduced for institutions such as check cashers,

and money exchange or remittance businesses. Finally in relation to supervision, MOT has been unable to conduct supervision due to lack of resources, and it is thus recommended that in order to ensure an efficient use of resources and to achieve greater clarity and consistency, the whole task of supervision be left to the CBA or other appropriate supervisory agency.

105. The active approach taken by Aruba has led to it being in substantial compliance with most of the FATF Forty Recommendations. Though there have been limited results to date, this has to be seen in the context of the size of the island and the newness of the system. Overall, many significant advances have been made. Once the recommendations referred to in the reports are in place, and the other current amendments completed, Aruba will need to focus its attention on the practical enforcement of the new laws and mechanisms. Overall, Aruba is to be commended for its active approach to combating money laundering, and it is hoped that continuing this approach will lead to significant results and effective system.

Netherlands Antilles (Kingdom of the Netherlands)

106. The most important criminal activity on the Netherlands Antilles stems from its role as a transit country for drug trafficking. Other predicate crimes that are of significant concern are trafficking in firearms, fraud and to a lesser extent, smuggling of products such as tobacco. There are also crimes which are of concern to particular islands within the Antilles e.g. St. Maarten is experiencing problems with establishments that offer internet gambling without a permit. Information is not available about the extent to which the Netherlands Antilles is used to launder the proceeds of crimes committed abroad, even though such proceeds are likely to be more substantial than the proceeds from crimes committed within the Netherlands Antilles. Similarly, the authorities were unable to provide details on the money laundering techniques and methods that are most prevalent in the Netherlands Antilles. It is therefore difficult to determine whether the amount of money being laundered has increased, and the degree to which the international payment system is being misused by money launderers in connection with the investment of illegitimate funds in the Netherlands Antilles or the layering of funds via accounts opened there.

107. Since the last evaluation the Netherlands Antilles has substantially implemented most of its anti-money laundering system. The MOT-NA was established in October 1996, and became operative a year later. In February 1996 the National Ordinance concerning the reporting of unusual transactions (the Reporting Ordinance) and the National Ordinance requiring identification when rendering financial services (the Identification Ordinance) were enacted. Both Ordinances came into effect in late 1997. A set of indicators was also prepared for the financial sector which lays out the unusual transactions which must be reported, and in November 1996, the Central Bank also issued a set of guidelines on the detection and deterrence of money laundering. The government is currently preparing new indicators, and is considering how to ensure that casinos and remittance agents apply the proper anti-money laundering standards.

108. The penal provisions concerning money laundering generally have a wide scope. The offence applies to all crimes, extends to cases where the defendant should reasonably have suspected that the money was from the proceeds of the crime, and the penalties should provide a significant disincentive. A weakness is that the offences are restricted to laundering money, securities and claims, thus excluding real or other personal property, which limits the scope of the offence. The fact that no prosecution or conviction for money laundering has taken place since the offences were enacted in 1993 indicates the offence may be difficult to prove. There are also some other technical uncertainties as to the scope of the offence, and these should be clarified and any weaknesses removed. The legislation dealing with confiscation, seizure and ancillary matters appears to be broad reaching, and potentially very effective. Apart from some minor refinements that may be required in relation to property held by third parties, the issue now is the practical application of the legislation. Similarly, new legislation has been introduced to substantially increase the possibilities for international mutual legal assistance. In June 1999, the Vienna Convention was put into force, and the 1990 Council of Europe Convention is expected to enter into

force on 8 July, 1999. At the level of informal co-operation, changes need to be made to make it easier for MOT-NA to exchange information directly with other FIUs, without requiring a formal treaty before this can take place.

109. MOT-NA has made considerable progress since it became operational in October 1997. However, the unusual transaction reporting system is a complex and potentially time intensive system. It is very important in a small jurisdiction that the system is an efficient one, and the lack of computerisation in the Netherlands Antilles does cause delays and additional unnecessary costs. Manual inputting of unusual transaction reports, having to visit the police and manually compare files on a confidential basis, and visiting and searching public registers is a slow and inefficient method of analysing and processing reports. The priority should be to make the existing processing system more efficient and effective.

110. The BFO and the special public prosecutor with responsibility for the money laundering cases, combined with the larger RST unit, should provide a significant impetus and source of expertise for law enforcement efforts against money laundering and the proceeds of crime. However, the fact that money laundering investigations are confined to cases resulting from STRs, combined with the lack of statistics and results on confiscation suggests that a more proactive approach to money laundering and the proceeds of crime and the use of new investigative techniques is required. Customs currently has a limited role to play, but when the cross border declaration system is introduced, it should be complemented by increased powers for Customs officers to play a full role in implementing the system and working with the police and MOT-NA to prevent cross border cash money laundering.

111. The Identification and Reporting Ordinances, and the Guidelines issued by the Central Bank provide a very sound foundation for the anti-money laundering measures in the financial sector, and the measures are in place and operational in the banking sector. However important further measures are still required in relation to some categories of NBFI and the offshore sector, where there has been a lack of reports, and the CIWG and MOT-NA will need to address this issue is the context of broader controls outside the banking sector. There is also limited guidance outside credit institutions, and proper supervisory checks or controls are poor or non-existent for institutions such as unlicensed money remitters, casinos and the offshore sector (other than offshore banks and associated trust companies). The CIWG should take steps to identify the participants in these types of businesses, and to implement appropriate control mechanisms, guidelines and training.

112. Another significant concern relates to companies and foundations incorporated in the Netherlands Antilles, the difficulties in identifying the beneficial owner of property, and the unsupervised role of lawyers, accountants, and many trust companies in providing services to non-residents. Although the members of the VOB have signed onto a voluntary code of conduct that includes customer identification provisions based on the Basle Principles, and entities opening bank accounts in the Netherlands Antilles are thereby subject to applicable customer identification provisions, trust companies do not generally fall under the Identification or Reporting Ordinances. The government needs to ensure that: (a) participants in the offshore sector are subject to binding obligations to identify customers, keep records, report unusual transactions etc; (b) there are appropriate controls on the entry of trust companies and other firms into the industry; and (c) there is instituted a manageable system to supervise or at least independently audit those firms to check that they are complying with their obligations. Though the risks are not as significant, similar concerns regarding lack of internal controls, supervision, money laundering awareness and training, also apply to casinos and the Free Trade Zone. A number of fundamental steps concerning supervision and control are needed for reasons not just restricted to money laundering, and whilst pursuing these policy initiatives, it should also produce more detailed proposals for a cross border currency reporting regime, which could be implemented in due course.

113. Overall, considerable efforts have been made in the last four years and important steps towards compliance with the FATF forty Recommendations have been taken. Though much of the system is very recent, the penal legal system is nearly in place, an operational structure is established and the basic preventive measures are now in place in the banking sector. Though further refinements are required and additional measures are necessary in relation to NBFI and non-financial businesses, particularly the offshore sector, further experience is needed before a complete assessment can be made of the effectiveness of the system as a whole.

C. APPLICATION OF THE POLICY FOR NON-COMPLYING MEMBERS

(i) Principles

114. Peer pressure is enhanced by the FATF's policy for dealing with members which are not in compliance with the forty Recommendations. The measures contained in this policy represent a graduated approach aimed at enhancing peer pressure on members to take action to tighten their anti-money laundering systems.

(ii) Steps applied in 1998-1999

Austria

115. Following Austria's failure during FATF-IX to alter its position in relation to anonymous passbook savings accounts for Austrian residents, it was decided to send a high level mission to Vienna in order to reinforce the concerns of the FATF regarding the passbooks. The mission, led by the FATF President, took place in mid-September 1998 and met with Mr. Edlinger, the Austrian Minister of Finance, and other high level Austrian officials. The Minister was advised of the concerns within the FATF at the continued retention of anonymous passbooks for Austrian residents and Austria's failure to comply with FATF Recommendations 2 and 10. The members of the mission were informed that anonymous passbooks were a very sensitive issue in Austria. They were also informed of the ongoing infringement procedures with regard to anonymous accounts in Austria initiated by the EC on the basis of the European Union Directive 91/308/EEC on prevention of the use of the financial system for the purpose of money laundering. Minister Edlinger also stated that Austria would naturally respect the judgement of the European Court of Justice when it was handed down.

116. At the FATF Plenary meeting in September 1998, Austria advised the FATF that in relation to anonymous securities accounts, since 1 August 1996 no new accounts can be opened. Securities from existing accounts can be sold anonymously whereas acquisitions of additional securities for "old" anonymous securities accounts require prior identification. Austria also stated that the Penal Code would be amended from 1 October 1998 to remove the ATS 100,000 threshold for the money laundering offence and to add new predicate offences. Although no change had occurred in relation to the anonymous passbook accounts, the matter was deferred until the February 1999 Plenary in order to give Austria a reasonable time to consider what action it might take.

117. At the February 1999 meeting, Austria advised that no changes had been made or were proposed regarding anonymous passbooks. Following concerns expressed regarding the closure of anonymous accounts and payments made by bank cheque, Austria provided guidance aimed at preventing persons from closing anonymous passbook accounts and asking for a bank cheque with the balance of the account. All payments from an anonymous passbook can now only be made by cash.

118. However, considerable concern still exists regarding the actual and potential misuse of anonymous passbooks by money launderers, Austria's consequent failure to comply with two important FATF Recommendations, and its failure to take or propose any action to deal with the situation. A public statement was therefore issued under Recommendation 21, pursuant to the non-compliance procedures of the FATF, calling on Austria to remove anonymous passbooks accounts, and warning financial institutions of the risks that are associated with such accounts.

Canada

119. Following the discussion of its mutual evaluation report in 1997, Canada provided a progress report at the June 1998 FATF Plenary meeting setting out proposals for a range of new anti-money laundering measures. The most important of these are a mandatory suspicious transaction reporting (STR) system, a reporting system for the cross-border movements of large amounts of currency and monetary instruments and the establishment of a financial intelligence unit (FIU) which would receive all STRs, and cross-border reports, and information from foreign FIUs. A number of other measures including new regulations and guidelines to strengthen the financial system were also proposed.

120. Canada completed an eight-month period of public consultation on the proposed new system in February 1999, and on 31 May 1999 a Bill was tabled in Parliament which addresses the three major measures set out above:

- regulated financial institutions, casinos, bureaux de change and other bodies or persons which act as financial intermediaries, e.g., lawyers or accountants, will be required to report suspicious transactions;
- persons or entities which carry large amounts of currency or monetary instruments into or out of Canada will be required to report this to customs officials;
- the Financial Transactions and Reports Analysis Centre of Canada will be established to receive and analyse reported and other information, and to disclose prescribed information to designated agencies to support law enforcement.

121. In addition, draft regulations addressing issues of customer identification and the coverage of the existing regulations have been prepared and consultation will take place with concerned parties during the Northern hemisphere summer and fall.

Japan

122. Following the discussion of its second mutual evaluation report at the June 1998 Plenary meeting, which concluded that the current Japanese money laundering system was not effective in practice, the delegation of Japan reported back to the FATF on the measures it had taken to improve its regime since that date.

123. The Anti-Organised Crime Bills, which contain several significant counter-measures (extension of the list of predicate offences, value based confiscation system, establishment of a financial intelligence unit in the Financial Supervisory Agency, electronic surveillance systems), was passed on 1 June 1999 by the House of Representatives. In addition, the Japanese authorities had already undertaken some work in relation to the establishment of an FIU (the creation of an office within the Financial Supervisory Agency for the purpose of establishing the FIU, the preparation of guidelines to increase the level of suspicious transactions reports, the organisation of seminars and meetings with financial institutions and the development of specific software).

Singapore

124. It was suggested during the discussion of the second mutual evaluation report on Singapore in February 1999 that Singapore provide a progress report, in view of serious concerns over its failure to comply, or to comply fully, with a number of the forty Recommendations. In particular, concern was expressed regarding the lack of significant progress since the first evaluation in implementing new and more effective measures. The main weaknesses concerned the need to apply all the relevant measures not only to drug trafficking but to a range of other serious crimes; the necessity for clear and comprehensive mutual legal assistance legislation, combined with a range of treaties; and the desirability of making the legal and administrative system for suspicious transaction reporting significantly more efficient and effective.

125. At the June 1999 Plenary, Singapore advised that it had tabled a Bill in its Parliament on 4 May 1999 which amended the Drug Trafficking (Confiscation of Benefits) Act. The Bill is scheduled to be presented for the Second and Third Readings on 6 July 1999. The main points contained in the Bill are:

- the extension of the crime of money laundering and of confiscation laws to a range of serious offences;
- reducing the mental standard to prove the offence to "reasonable grounds to believe";
- creating an obligation for all persons who, in the course of their employment, suspect that property relates to the proceeds of crime, to report this to the competent authority;
- making it easier to provide assistance to foreign authorities, by lowering the threshold from "prima facie case" to "reasonable grounds for suspecting"; and
- a number of technical amendments to the confiscation provisions.

126. In addition, the Bill will amend the Extradition Act to make serious crimes money laundering offences extraditable. Singapore will also introduce a Mutual Legal Assistance Act by early 2000. In recognition of the important role played by an Financial Intelligence Unit, a dedicated FIU will be set up within the Commercial Affairs Department (CAD). To improve the transparency and efficiency of the suspicious transaction reporting procedure, Singapore has implemented a dual reporting system whereby financial institutions disclose suspicious transactions directly to the CAD and extend a copy to the financial regulatory authority.

D. OTHER MONITORING ASPECTS

(i) Voluntary reporting

United States

127. The second mutual evaluation of the United States was discussed and approved during FATF-VIII (1996-1997). At the time of the discussion and approval of the evaluation, the United States was not asked to provide any status report back to the Plenary. However, well over a year after discussion of this evaluation, the United States was asked by one jurisdiction to provide a status report with respect to recent initiatives regarding non-bank financial institutions. As the United States believes that it is important for all member nations to be as forthcoming and candid about their existing state of implementation as possible, it volunteered to report back to the Plenary.

128. On several occasions, the United States advised the FATF Plenary that it was continuing to work on the question of the regulation of non-bank financial institutions such as money remitters and exchange

offices, and that it had also been developing regulations which were at a draft stage. There are also Bills before the US Congress dealing with the forfeiture laws and with an extension of the types of foreign predicate offences which are the basis for a money laundering offence in the United States. The United States bank supervisory agencies also released a proposed regulation, entitled the "Know Your Customer" regulation, which would have standardised certain existing anti-money laundering procedures, including customer identification requirements and procedures, as well as existing statutory and regulatory obligations to identify and report unusual and suspicious transactions. Although the proposed "Know Your Customer" regulation has been withdrawn, the above-mentioned anti-money laundering requirements remain in place.

(ii) Gulf Cooperation Council

129. The Gulf Cooperation Council (GCC), which is in the unique position of being a member of FATF but with non-FATF member countries as its constituents, received a high-level FATF mission in January 1999 in Riyadh to discuss how to improve the implementation of effective anti-money laundering systems within the GCC members. This initiative also permitted a positive discussion with representatives of all the GCC States[6] on how to obtain more information on the state of their compliance with the forty Recommendations.

130. As a result, the GCC made the commitment that complete responses to self-assessment questionnaires would be provided to the FATF Secretariat together with copies of relevant laws and regulations, so that a comprehensive self-assessment survey for its member States could be discussed in September 1999. In addition, subject to confirmation, certain members of the GCC agreed to undergo a mutual evaluation. Finally, the GCC General Secretariat agreed to give clear and serious attention to the FATF's work and to strengthen its participation in FATF.

131. However, at the conclusion of the final Plenary meeting of FATF-X (30 June-2 July 1999), only three responses (Bahrain, Qatar, United Arab Emirates) to self-assessment questionnaires had been provided to the FATF Secretariat and none of the relevant documentation. This situation may impede the preparation of the aforementioned survey. While the Plenary meeting was encouraged by the official acceptance of the Saudi Government of the forty Recommendations, it was deeply concerned by the lack of progress towards the implementation of required evaluation of rules and regulations pertaining to money laundering in the Gulf States.

II. REVIEWING MONEY LAUNDERING METHODS AND COUNTER-MEASURES

132. The annual survey of money laundering methods and countermeasures provides a global overview of trends and techniques and focuses on selected major issues. Other areas of work included the role of the accounting profession and accounting rules in efforts to combat money laundering; the expansion of the G-7 Reference Guide to procedures and contact points on information exchange to financial regulators and law enforcement agencies; and the continuation of work on estimating the magnitude of money laundering. Finally, taking into account the work of the OECD's Committee on Fiscal Affairs, FATF started to consider how anti-money laundering systems can contribute to deal effectively with tax related crimes.

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[6] Bahrain, Kuwait, Oman, Qatar, Saudi Arabia and the United Arab Emirates.

A. 1998-1999 SURVEY OF MONEY LAUNDERING TRENDS AND TECHNIQUES

133. FATF typologies exercises provide a forum for the exchange of information and intelligence on current trends in money laundering and effective countermeasures. The exercises take place as an annual meeting of experts from FATF member law enforcement agencies and regulatory authorities. As has been mentioned before and as shown by the written submissions of the FATF delegations each year, the basic techniques and mechanisms for money laundering have been well documented. Continuing last year's effort to focus attention on areas that have not yet been fully developed, the FATF-X meeting examined four or five major topics, which then served as the basis for further discussion. The following paragraphs summarise the conclusion of this year's exercise.

134. One of the major topics of this year's meeting centred on the potential money laundering implications associated with the introduction of the euro. The critical time as far as risk is concerned is the period from January to June 2002, when euros in coin and paper form will replace national currencies. A number of experts believed that existing preventive measures had the potential risk of being overwhelmed by the increased burden of work for financial institution personnel during the changeover. The experts were also of the opinion, however, that the introduction of the euro might be an opportunity for detecting laundering activity. Although existing preventive systems should be adequate in detecting possible money laundering, a number of FATF members are taking extra steps to re-emphasise or reinforce their anti-money laundering programmes. The full report of FATF-X on typologies is at Annex C.

135. The less than adequate or lack of co-operation on the part of some countries or territories continues to be an area of concern to the experts. The inability to obtain relevant information on the beneficial owners of foreign legal entities represents one of the major roadblocks to successfully detecting, investigating and prosecuting suspected international money launderers. The abuse of new payment technologies by launderers also appears no longer to be a distant possibility, as a number of these systems — Internet banking was cited as one important example — move from the prototype and initial introduction to acceptance and widespread use by consumers. Awareness of the potential role of the gold market is growing among FATF member countries, and the experts have observed that transactions involving gold are increasingly found in money laundering schemes, particularly through the hawala / hundi parallel banking system.

136. The experts have observed a growing tendency for professional services providers, such as accountants, solicitors, company formation agents, and other similar professions, to be associated with more complex laundering operations. These professionals set up and often run the legal entities that lend the high degree of sophistication and additional layers of respectability to such money laundering schemes. Although a number of these professionals operate in certain offshore locations, other professionals often provide similar services within FATF member countries themselves. Only a few members impose obligations on professional services providers to report suspicious transactions. Those that do are not always satisfied with the amount of reporting from this sector; however, the quality of some individual reports, according to the experts, seems to justify the need for such reporting.

B. OTHER AREAS OF WORK

(i) Support of efforts to develop anti-money laundering standards and guidelines in the accounting field

137. Closer integration of relevant aspects of the FATF forty Recommendations into the work of accounting and auditing professionals would advance the significance and beneficial effect of the Recommendations. It would also contribute to extending anti-money laundering guidelines to financial systems that are not represented in FATF or regional FATF-style bodies. The FATF forty Recommendations emphasise the need for adequate record keeping, comprehensive controls and procedures within financial institutions to guard them against money laundering, and periodic reviews of the proper functioning of these controls and procedures. These are matters that clearly lend themselves to evaluation through the auditing process.

138. Therefore, FATF members agreed that the Task Force should be represented on a committee set up by the International Federation of Accountants (IFAC) for the purpose of establishing anti-money laundering standards and guidance for the accounting profession, that representatives from IFAC and other similar bodies should be invited to attend certain relevant FATF meetings as observers. It was also agreed that it would be useful for the accounting standard setting bodies**,** which are members of IFAC, to refer to the FATF Recommendations when developing such norms.

(ii) Strengthening international co-operation

139. In May 1998, the G7 issued a reference guide on procedures and points of contact for exchanging information. The guide set out the key features of each G7 country's privacy and secrecy laws, its ability to share information and the conditions under which such information may be shared, and each country's position on mutual legal assistance among other things. It provided an exhaustive list of contacts for financial regulators, law enforcement agencies, and relevant ministries, departments or administrative authorities. The guide also contained a set of scenarios that described how G7 countries would respond to particular situations or requests. The FATF Mandate for FATF-X called for creating a similar guide expanded to cover all FATF member countries and jurisdictions. Information was solicited from members during the subsequent year, and a preliminary draft was presented at the plenary meeting in Tokyo. Work will continue on the FATF Reference Guide into FATF-XI (July 1999 to July 2000).

(iii) Estimating the magnitude of money laundering

140. During 1998-1999 FATF work continued on estimating the magnitude of money laundering. The ad hoc group, chaired by the head of the United States delegation, considered the available studies that have been completed concerning estimation of the volume of criminal proceeds. The group recognised that the fundamental data necessary for this very complex study is often incomplete, or may be conflicting, and that further efforts will need to be made by all participating countries and international organisations.

141. It was agreed that initial efforts should concentrate on estimating the amount of criminal proceeds available in relation to a short list of serious profit generating crimes, but with a focus on the amount derived from drug trafficking. Once some progress had been made on this issue, then consideration could be given to the amount of such proceeds available for money laundering. A second meeting of experts from members and international organisations sponsored by the Chair of the ad hoc Group took place on 3-4 December 1998. The experts considered the methodologies that had been used, and the data sources that are available, with particular reference to calculating the proceeds of drug trafficking. The meeting heard presentations from Canada, Finland, Switzerland and the United States, and considered the difficulties that arise when comparing demand and supply side estimates because of intra-European transit of drugs.

142. The group decided that efforts should also be made to intensify contacts with other relevant international organisations, and particularly those which work to combat the supply of, and demand for

illicit drugs. The ad hoc group further developed its relations with the UNDCP, and created new contacts with Europol and the European Monitoring Centre for Drugs and Drug Addiction. It is recognised that the complex questions concerning the availability, reliability and comparability of data, and of the appropriate methodology, require intensified efforts and greater co-operation with all the international experts in this field. Despite the difficulties, it was agreed that the FATF should continue to develop this study and that all FATF member jurisdictions should participate. The study will therefore continue during FATF-XI, and will focus on gathering the available national and international data, particularly in relation to drug trafficking, and providing an interim report on the state of information regarding drug trafficking proceeds for the June 2000 Plenary.

(iv) Capacity of anti-money laundering systems to deal effectively with tax related crimes

143. Further to the conclusions of the May 1998 G-7 meeting of Finance Ministers, FATF considered how anti-money laundering systems can contribute to deal effectively with tax related crimes. Work referred to by the G-7 in this area was based on furthering the following objectives:

(i) Effective anti-money laundering systems must ensure that obligations to report transactions relating to suspected criminal offences continue to apply even where such transactions are thought to involve tax offences.

(ii) Money laundering authorities should be permitted, to the greatest extent possible, to pass information to their tax authorities to support the investigation of tax related crimes, and such information should be communicated to other jurisdictions in ways which would allow its use by their tax authorities. Such information should be used in a way which does not undermine the effectiveness of anti-money laundering systems.

144. With regard to the first objective, it was recognised that there was a need to address a potential weakness in money laundering reporting systems, namely that criminals can avoid suspicious transactions reporting requirements by stating that their affairs relate only to tax matters (the so-called "fiscal excuse"). Therefore, in order to help close this loophole, FATF members adopted the following Interpretative Note to Recommendation 15:[7]

> "In implementing Recommendation 15, suspicious transactions should be reported by financial institutions regardless of whether they are also thought to involve tax matters. Countries should take into account that, in order to deter financial institutions from reporting a suspicious transaction, money launderers may seek to state *inter alia* that their transactions relate to tax matters."

145. As for the second objective, some representatives of the FATF and the OECD Committee on Fiscal Affairs (CFA), held an informal contact meeting in January 1999 to consider how anti-money laundering systems can deal effectively with tax related crimes. Both the CFA and the FATF concurred that it would be useful to continue this exchange of views particularly on the issue of the provision of information to tax authorities without undermining the effectiveness of anti-money laundering systems, and that another informal meeting would take place in February 2000.

III. FATF MEMBERSHIP AND OUTREACH ACTIVITIES

[7] Recommendation 15: "If financial institutions suspect that funds stem from a criminal activity, they should be required to report promptly their suspicions to the competent authorities."

146. As the third component of its mission, the FATF undertakes external relations actions designed to raise awareness in non-member nations or regions of the need to combat money laundering, and offers the forty Recommendations as a basis for doing so. In promoting the adoption of anti-money laundering measures, it is important to bear in mind that the FATF does not act in a vacuum. A number of international organisations or bodies play a significant role in this respect. The following paragraphs describe the most important developments which occurred in 1998-1999 in the international fight against money laundering.

147. The FATF continued to collaborate with the relevant international organisations/bodies rather than launch new initiatives. The Task Force participated in anti-money laundering events organised by other bodies in order to follow the developments taking place in non-members and in particular the adoption of money laundering counter measures. To increase the effectiveness of international anti-money laundering efforts, the FATF and the other organisations and bodies endeavour to co-ordinate their activities through an annual co-ordination meeting and meetings of regional ad hoc groups (Asia/Pacific, Caribbean and Latin America, Central and Eastern Europe) which take place in the margins of the FATF Plenaries.

148. However, in line with its new strategy for spreading the anti-money laundering message throughout the world, FATF has now started to deal with the expansion of its membership. In addition, FATF launched an important exercise concerning the issue of non-cooperative countries and territories.

A. FATF MEMBERSHIP

149. The FATF has decided to expand its membership to a limited number of strategically important countries which could play a major role in their regions in the process of combating money laundering.

150. The minimum and *sine qua non* criteria for admission are as follows:

- to be fully committed at the political level: (i) to implement the 1996 Recommendations within a reasonable timeframe (three years), and (ii) to undergo annual self-assessment exercises and two rounds of mutual evaluations;

- to be a full and active member of the relevant FATF-style regional body (where one exists), or be prepared to work with the FATF or even to take the lead, to establish such a body (where none exists);

- to be a strategically important country;

- to have already made the laundering of the proceeds of drug trafficking and other serious crimes a criminal offence; and

- to have already made it mandatory for financial institutions to identify their customers and to report unusual or suspicious transactions.

151. According to the objectives decided upon in the review of the FATF's future, the work related to enlarging FATF membership was launched in 1998-1999. The FATF adopted a policy on membership defining the process for admission and the rights and obligations of new observer members. It was recognised that potential new members should belong to areas where FATF is not sufficiently represented, and that there was a need to maintain a certain level of geographical balance.

152. Rather than waiting for applications, it was believed that FATF should take a more proactive approach. Enlargement of the membership was therefore initiated by informal contacts between FATF members and several target countries. As a result, in June 1999, following their written political commitment to endorse the forty Recommendations, to undergo two mutual evaluations and to play an active role in their region, it was decided that three strategically important countries (Argentina, Brazil and Mexico) will be invited to join the FATF as observers and to attend the next Plenary meeting in September 1999 in Portugal. FATF will continue to address the issue of new members in 1999-2000.

B. NON-COOPERATIVE COUNTRIES OR TERRITORIES

153. A number of countries and territories, including some financial offshore centres, continue to offer excessive banking secrecy and allow shell companies to be used for illegal purposes. The Task Force has therefore decided to carry out further work in this field, i.e. what can be done to deal with the abuses. In this context, the FATF has started to consider proposals on the steps to be taken regarding countries and territories which fail to provide effective international administrative and judicial co-operation in money laundering cases.

154. To deal with the issue, FATF established an ad hoc group to discuss in more depth the steps to be taken regarding these non-cooperative jurisdictions including some offshore financial centres. In addition, the annual FATF typologies exercise (review of money laundering trends) addressed the issue in preparation for the work of the ad hoc group.

155. The scope of the group's work covers all significant financial centres, both inside and outside FATF membership. A priority task of the ad hoc group is to define the detrimental rules and practices which impair the effectiveness of money laundering prevention and detection systems, as well as the success of judicial enquiries in this area, so as to determine criteria for defining the non-cooperative countries or territories. A second step is to identify the jurisdictions which meet the above criteria. The third step consists in reviewing and agreeing the necessary international action to encourage compliance by the identified non-cooperative jurisdictions. Finally, FATF needs to assess whether the forty Recommendations contain the appropriate counter-measures in the area of non-cooperation.

156. Priority has thus been given to gaining approval of a precise list of criteria which would specify the difficulties experienced with non-cooperative countries or territories. The proposed criteria cover prevention, detection and penal provisions, and they include such items as financial regulations (e.g. supervision of financial institutions, excessive secrecy, customer identification requirements and other regulatory requirements), judicial and administrative international co-operation, and the issue of resources.

157. This important work is making steady progress. The elaboration of criteria is expected to be finalised later this year, so that work on the identification of jurisdictions which meet those criteria can begin during FATF-XI.

C. INTERNATIONAL ANTI-MONEY LAUNDERING INITIATIVES

(i) FATF's external relations action

Black Sea Economic Cooperation

158. The FATF organised a Money Laundering Seminar for the countries of the Black Sea Economic Cooperation (BSEC)[8] with the support of the Greek Ministry of National Economy. This Seminar took place on 21-22 October 1998 in Athens and was attended by fifteen countries from BSEC and FATF and three international organisations. Representatives at the Seminar shared their experiences in combating money laundering and discussed the various measures adopted by their countries to combat this threat. The Seminar heard reports from member countries of the BSEC on progress made in enacting anti-money laundering legislation since the first seminar in 1996. While there was a marked difference from country to country, an increasing number of countries were in the process of enacting legislation.

159. The BSEC member countries agreed to implement anti-money laundering measures based on the FATF Recommendations, and on the following international agreements: the United Nations Convention against Illicit Traffic in Narcotic Drugs and Psychotropic Substances (the "Vienna Convention" of 1988); the Council of Europe Convention on Laundering, Search, Seizure and Confiscation of the Proceeds from Crime (the "Strasbourg Convention" of 1990); and the European Union 1991 Directive on Prevention of the Use of the Financial System for the purpose of Money Laundering.

(ii) Anti-money laundering activities of "FATF-style" regional and other bodies

Caribbean Financial Action Task Force

160. Since its inception, membership in the Caribbean Financial Action Task Force **(**CFATF) has grown to twenty-five States of the Caribbean basin.[9] The CFATF has instituted measures to ensure the effective implementation of, and compliance with, the nineteen CFATF and forty FATF Recommendations. The CFATF monitors members' implementation of the Kingston Ministerial Declaration through the following activities:

- self-assessment of the implementation of the Recommendations;
- an on-going programme of mutual evaluation of members;
- co-ordination of, and participation in, training and technical assistance programmes;
- plenary meetings twice a year for technical representatives; and
- annual Ministerial meetings.

161. CFATF member governments have made a firm commitment to submit to mutual evaluations of their compliance both with the Vienna Convention and with the CFATF and FATF Recommendations. This firm commitment was signalled by the decision, made in October 1997 by the CFATF Council of Ministers in Barbados, to adopt a mandatory schedule of mutual evaluations. According to this schedule, the CFATF's first round of mutual evaluations will be completed by the year 2000.

162. In May 1999, the CFATF, in conjunction with the French *Centre interministériel de formation anti-drogue* (CIFAD), organised in Martinique a training seminar for experts who would be participating as evaluators in the mutual evaluation process. This event, which was well attended by participants from CFATF jurisdictions, discussed the applicable international conventions and instruments, the practical

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[8] Member countries of BSEC are: Albania, Armenia, Azerbaijan, Bulgaria, Georgia, Greece, Moldova, Russian Federation, Romania, Turkey and Ukraine.

[9] The current CFATF members are: Anguilla, Antigua and Barbuda, Aruba, the Bahamas, Barbados, Belize, Bermuda, the British Virgin Islands, the Cayman Islands, Costa Rica, Dominica, Dominican Republic, Grenada, Jamaica, Montserrat, the Netherlands Antilles, Nicaragua, Panama, St. Kitts and Nevis, St. Lucia, St. Vincent and the Grenadines, Suriname, Turks and Caicos Islands, Trinidad and Tobago and Venezuela.

aspects of the process, and the legal, financial and law enforcement components of anti-money laundering systems.

163. The FATF supports the significant progress which has been made by the CFATF under both the chairmanships of Barbados and the Cayman Islands. The CFATF also pursued its active typologies programme and the development of important internal processes. Three further mutual evaluation reports were discussed (Bahamas, the Dominican Republic, St. Vincent and the Grenadines) and three on-site visits took place (St. Kitts and Nevis, Jamaica and Dominica) in 1998-1999. However, Antigua and Barbuda, prior to the March 1999 CFATF Plenary in which its mutual evaluation was to be discussed, did not provide comments on the draft report, thereby impeding discussion of its mutual evaluation. In addition, recent legislative and other changes seriously weakened Antigua and Barbuda's anti-money laundering regime. The FATF consulted with CFATF representatives on the issue during the June 1999 Plenary. At that meeting, FATF members agreed that the FATF President should write to the CFATF Chairman expressing their concerns, and the FATF transmitted such a letter.

Asia/Pacific Group on Money Laundering

164. The Asia/Pacific Group on Money Laundering (APG) currently consists of 16 members[10] in the Asia/Pacific region comprising members from South Asia, Southeast and East Asia and the South Pacific. In March 1998, the first annual meeting of the APG was held in Tokyo and attended by twenty-five jurisdictions from the region. A revised Terms of Reference was agreed upon, as well as an action plan for the future which is aimed at the effective implementation of the accepted international standards against money laundering as set out in the FATF's Recommendations.

165. The APG conducted two typologies workshops: in October 1998 in New Zealand, concentrating on offshore centres, and in March 1999 in Japan, addressing the issue of underground banking systems and money laundering. Representatives in attendance from offshore financial centres in the Pacific recognised the need to apply effective anti-money laundering measures especially in regard to information exchange and bank secrecy. A significant outcome of the March workshop was the creation of a working group which will study the problem of underground banking in more depth. The APG also conducted its first self-assessment exercise, on the basis of questionnaires modelled on those of the FATF, the results of which will be discussed at its next annual meeting, to take place in Manila in August 1999.

Council of Europe (PC-R-EV)

166. The Select Committee of experts on the evaluation of anti-money laundering measures (PC-R-EV) was established in September 1997 by the Committee of Ministers of the Council of Europe, to conduct self and mutual assessment exercises of the anti-money laundering measures in place in the twenty-two Council of Europe countries which are not members of the Financial Action Task Force.[11] The PC-R-EV is a sub-committee of the European Committee on Crime Problems of the Council of Europe (CDPC).

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[10] The members of the APG are: Australia; Bangladesh; Chinese Taipei; Fiji; Hong Kong, China; India; Japan; New Zealand; the People's Republic of China; Republic of Korea; Republic of the Philippines; Singapore; Sri Lanka; Thailand; United States of America and Vanuatu.

[11] The membership of the Committee is comprised of the Council of Europe member States which are not members of the FATF: Albania, Andorra, Bulgaria, Croatia, Cyprus, Czech Republic, Estonia, Georgia (since May 1999), Hungary, Latvia, Liechtenstein, Lithuania, Moldova, Malta, Poland, Romania, Russian Federation, San Marino, Slovakia, Slovenia, "The Former Yugoslav Republic of Macedonia" and Ukraine.

167. At its December 1998 Plenary meeting, the PC-R-EV adopted a procedural paper setting out fully the steps in the mutual evaluation process and a procedure for dealing with members which are not in compliance. Thus, the PC-R-EV now has in place a clear reference document which aims to bring consistency and an even-handed approach to the mutual evaluation process. At the same meeting, the PC-R-EV held its first typologies exercise on the theme of cash money laundering. The PC-R-EV intends similar exercises to become an annual feature of its activities.

168. During 1998-1999, ten on-site evaluation visits took place: Slovenia, Cyprus, Czech Republic, Slovakia, Malta, Hungary, Lithuania, Andorra, Romania and Poland. Mutual evaluation reports for the first eight of these countries were adopted by the Plenary meetings.[12] Twelve PC-R-EV countries have contributed experts to evaluation teams. Where a PC-R-EV member State undergoing evaluation is also a member of the Offshore Group of Banking Supervisors (OGBS), an expert from OGBS has accompanied the evaluation team. The OGBS participated in the evaluations of Cyprus and Malta during 1998. Each evaluation team has also been assisted by two experts from FATF countries. Twelve FATF countries have therefore been represented in PC-R-EV evaluations.

169. While continuing its work on mutual evaluations, the PC-R-EV will concentrate next year on extending the number of its member countries which contribute evaluators to the process; widening the pool of suitably experienced evaluators within the PC-R-EV countries; further improving the quality of the process and the product; and building on the work of the first typologies exercise. In this way, the Council of Europe will contribute fully and effectively to the development of the world-wide anti-money laundering network.

Offshore Group of Banking Supervisors

170. The conditions for membership of the Offshore Group of Banking Supervisors (OGBS) include a requirement that a clear political commitment be made to implement the FATF's forty Recommendations. In addition, the following members of the OGBS, which are not members of the FATF or the CFATF, are formally committed to the forty Recommendations through individual Ministerial letters sent to the FATF President during 1997-1998: Bahrain, Cyprus, Gibraltar, Guernsey, Isle of Man, Jersey, Malta, Mauritius and Vanuatu.

171. The OGBS is taking steps to carry out its first mutual evaluations during the summer of 1999; these will concern Jersey, Guernsey and the Isle of Man. Two other members of the OGBS -- Cyprus and Malta -- were covered in 1998-1999 by a joint Council of Europe/OGBS mutual evaluation.

(iii) Other international anti-money laundering action

United Nations

172. The United Nations has started the negotiation of a draft convention on transnational organised crime. The discussions on this issue, which began in early 1999, will lead to the adoption of a comprehensive set of measures to improve international co-operation against organised crime in November 2000. Among the important provisions of the draft convention are measures against money

[12] The summaries of the evaluation reports and the first Annual Report of the PC-R-EV can be obtained from the PC-R-EV Secretariat at the Council of Europe, F-67075 Strasbourg Cedex, France.

laundering. These provisions underwent a first round of discussions in April 1999 and will be further negotiated during the course of 1999. In particular, the draft convention currently contains an article requiring nations to criminalise money laundering (Article 4). The FATF endorses the requirement that all countries criminalise money laundering for appropriate serious offences. The draft convention also contains two options for an article requiring nations to take steps to institute comprehensive anti-money laundering domestic regulatory and supervisory regimes (Article 4 bis). The FATF strongly endorses the current option 2 of Article 4 bis and attaches specific importance to the text stating that "State Parties shall adopt and adhere to the international standards set by the Financial Action Task Force on Money Laundering…".

173. The Global Programme against Money Laundering (GPML) is a research and technical co-operation initiative implemented by the UN Office for Drug Control and Crime Prevention (ODCCP). Its aim is to increase the effectiveness of international action against money laundering through comprehensive technical co-operation services offered to Governments. The Programme is carried out in co-operation with other international and regional organisations. In the context of the GPML, the UNODCCP organised several anti-money laundering training and technical co-operation seminars.

Organization of American States/Inter-American Commission for Drug Abuse Control (OAS/CICAD)

174. The CICAD Group of Experts to Control Money Laundering has continued to monitor implementation of the Buenos Aires Plan of Action.[13] The CICAD Group of Experts, which meets twice a year, carried out a typologies exercise and completed its amendments to the OAS Model Regulations, including, *inter alia*, provisions to criminalise the laundering of proceeds not simply from drug trafficking offences but also from "serious crimes". The CICAD Secretariat has also co-sponsored and co-ordinated a number of training seminars involving anti-money laundering measures. Created in 1998, a CICAD working group is developing a Multilateral Evaluation Mechanism to evaluate the effectiveness of anti-drug and related arrangements, including work on indicators on the effectiveness of certain anti-money laundering measures.

Various international anti-money laundering events

175. In December 1998, several FATF members and the Secretariat participated in an international Money Laundering Seminar organised in Brasilia by the Central Bank of Brazil and the Brazilian Superior Court of Justice, on the occasion of the new Brazilian legislation. During 1998-1999, the FATF participated in several other anti-money laundering events, including the 8th international meeting on Assets Derives from Crime of the FOPAC Group of Interpol in Lyons in October 1998, a Seminar for Egyptian experts and government officials on "Fighting Organised Crime and Money Laundering" organised by the International Institute of Higher Studies in Criminal Sciences (ISISC) in Syracuse in November 1998, and the UN Crime Prevention and Criminal justice Commission Experts Group meeting on Corruption and its international financial channels, held in Paris at the French Ministry of Economy,

[13] In December 1995, the Ministers responsible for addressing money laundering in the States of the Western hemisphere met in Buenos Aires where they endorsed a Statement of Principles to combat money laundering and agreed to recommend to their Governments a Plan of Action reflecting this Statement of Principles for adoption and implementation. The Plan of Action specifically provided that the Governments intended to institute on-going assessments of the implementation of the Plan of Action within the framework of the OAS. This and other activities identified in this Plan were remitted to the CICAD for action.

Finances and Industry, in March 1999. Finally, FATF was also represented at the VII Plenary of the Egmont Group[14] held in Bratislava in May 1999.

CONCLUSION

176. During 1998-1999, further progress was again made in combating money laundering, both within and outside the FATF membership. However, ten years after the establishment of the Task Force, the need for continued mobilisation at the international level to deepen and widen the fight against money laundering is obvious. To this end, the FATF will continue to work with the relevant international organisations to foster the establishment of a world-wide anti-money laundering network, based on an adequate expansion of the FATF membership and the development of the FATF-style regional bodies.

177. Moreover, it will also be essential to continue to carry out in-depth analysis of money laundering trends and counter-measures in order to maintain the FATF's authority on international anti-money laundering policies. In addition, improving the effective implementation of the forty Recommendations within the FATF membership remains, more than ever, a critical challenge.

178. As the worldwide mobilisation against money laundering is the priority goal of the FATF, outreach action and enlarging the membership will continue to be given a high priority in the forthcoming years. This vital task will be carried forward in 1999-2000 under the Presidency of Portugal.

[14] The Egmont Group is the informal international grouping, set up in 1995, which provides a forum for financial intelligence units (FIUs) to improve support to their respective national anti-money laundering programmes. Forty eight FIUs are currently represented within the Egmont Group.

FATF-X

FINANCIAL ACTION TASK FORCE ON MONEY LAUNDERING

1998-1999 ANNUAL REPORT

ANNEXES

ANNEX A - List of countries and territories which have undergone a mutual evaluation

ANNEX B - Summary of compliance with the forty Recommendations

ANNEX C - 1998-1999 Report on Money Laundering Typologies

July 1999

ANNEX A

LIST OF COUNTRIES AND TERRITORIES WHICH HAVE UNDERGONE A MUTUAL EVALUATION

The purpose of this list is to make public the countries and territories which are either members of the Task Force or an FATF-style regional body, and which have undergone a mutual evaluation of their anti-money laundering system according to a process endorsed by the FATF. The list only includes the completed mutual evaluations (i.e. with final mutual evaluation reports endorsed by the respective plenaries of the relevant bodies). It is, of course, planned that this list will be updated as the mutual evaluation procedures of the various anti-money laundering bodies develop.

FATF (two rounds of mutual evaluations completed)[15]

Australia; Austria; Belgium; Canada; Denmark; Finland; France; Germany; Greece; Hong Kong, China; Iceland; Ireland; Italy; Japan; Luxembourg; the Kingdom of the Netherlands; New Zealand; Norway; Portugal; Singapore; Spain; Sweden; Switzerland; Turkey; the United Kingdom and the United States.

CFATF[16] (first round of mutual evaluations in progress)

Aruba,[3] the Bahamas, Barbados, the Cayman Islands, Costa Rica, Dominican Republic, the Netherlands Antilles,[17] Panama, Trinidad and Tobago.

Council of Europe PC-R-EV[18] (first round of mutual evaluations in progress)

Andorra, Slovenia, Cyprus,[19] Czech Republic, Hungary, Lithuania, Slovakia and Malta.[5]

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15 FATF members have agreed to undergo a third round of mutual evaluations starting in 2001.

16 The current members of CFATF are: Anguilla, Antigua and Barbuda, Aruba, the Bahamas, Barbados, Belize, Bermuda, the British Virgin Islands, the Cayman Islands, Costa Rica, Dominica, Dominican Republic, Grenada, Jamaica, Montserrat, the Netherlands Antilles, Nicaragua, Panama, St. Kitts and Nevis, St. Lucia, St. Vincent and the Grenadines, Suriname, Turks and Caicos Islands, Trinidad and Tobago and Venezuela.

17 As separate constituent parts of the Kingdom of the Netherlands, Aruba and the Netherlands Antilles have undergone two mutual evaluations by FATF evaluation teams, with the participation of CFATF for their second examination.

18 The current members of the PC-R-EV are: Council of Europe member States which are not members of the FATF: Albania, Andorra, Bulgaria, Croatia, Cyprus, Czech Republic, Estonia, Georgia (since May 1999), Hungary, Latvia, Liechtenstein, Lithuania, Moldova, Malta, Poland, Romania, Russian Federation, San Marino, Slovakia, Slovenia, "The Former Yugoslav Republic of Macedonia" and Ukraine.

3. Joint Council of Europe/OGBS (Offshore Group of Banking supervisors) evaluation.

ANNEX B
SUMMARY OF COMPLIANCE WITH THE FORTY RECOMMENDATIONS

Chart 1

Compliance with the FATF Forty Recommendations
1998-1999 Self-Assessment Survey
— Legal Issues
(13 Recommendations)

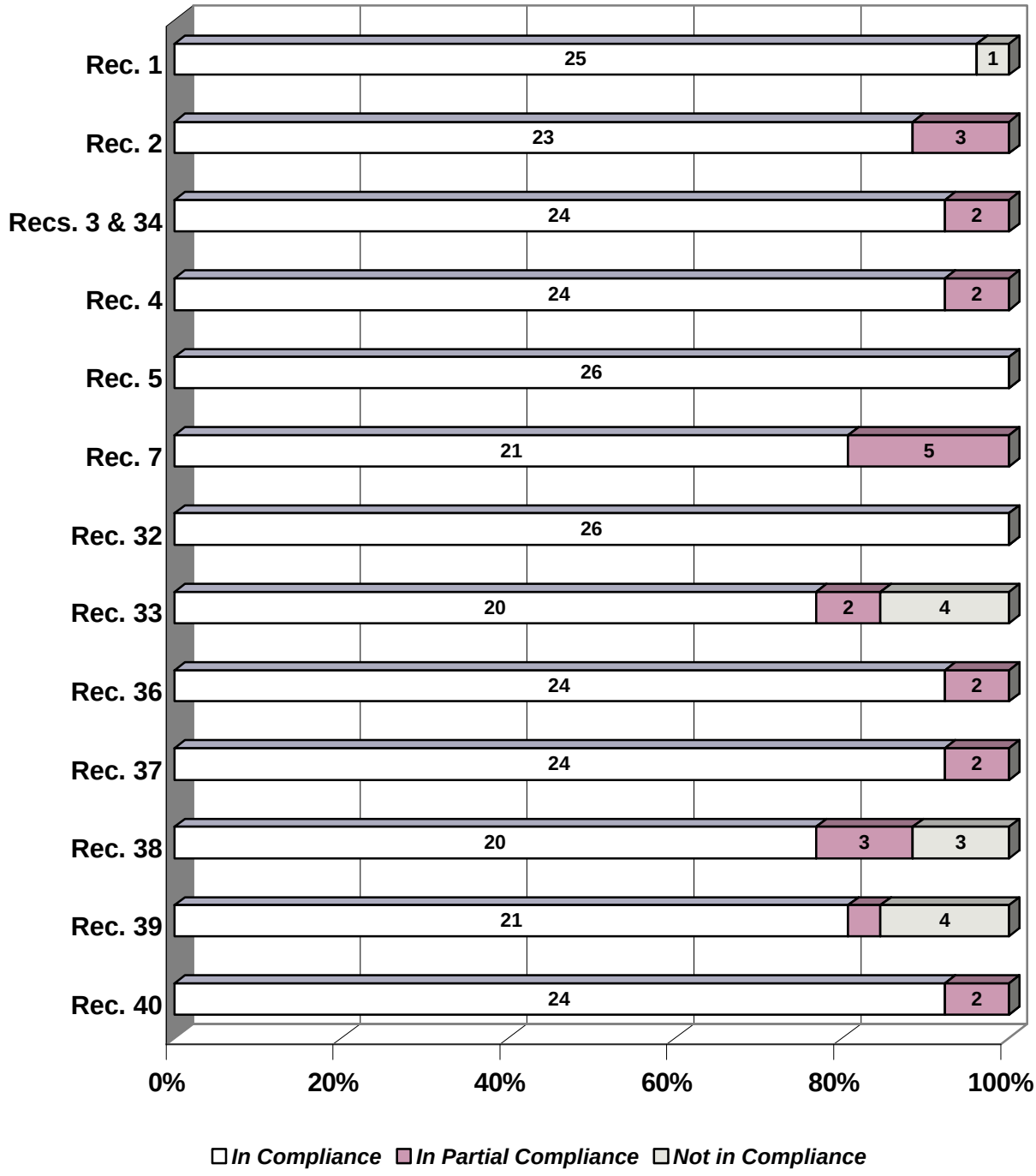


Chart 1 (a)

Compliance with the FATF 40 Recommendations
1998-1999 Self-Assessment Survey
— Financial Issues
(24 Recommendations)

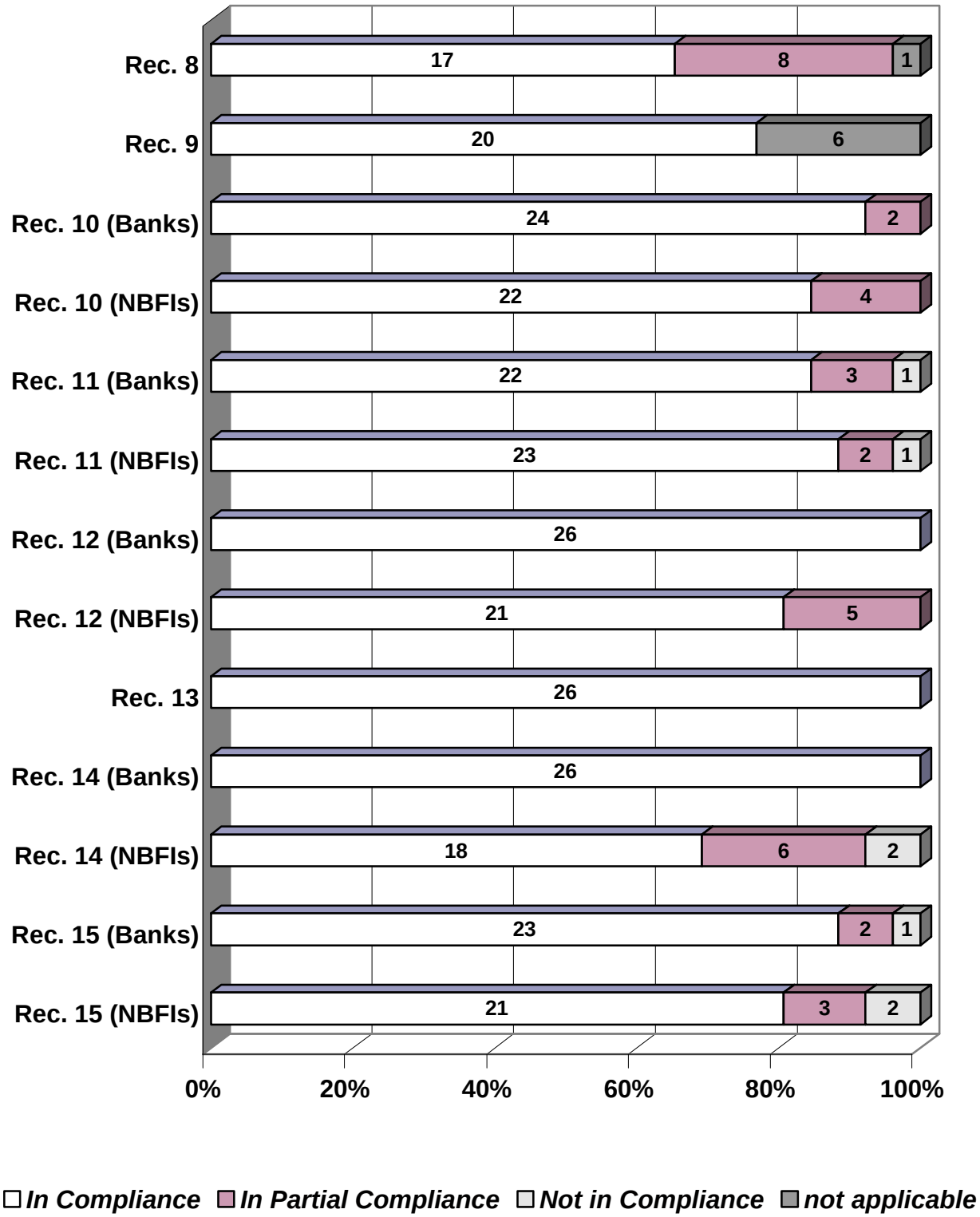


Chart 1 (b)

Compliance with the FATF 40 Recommendations
1998-1999 Self-Assessment Survey
— Financial Issues
(24 Recommendations — continued)

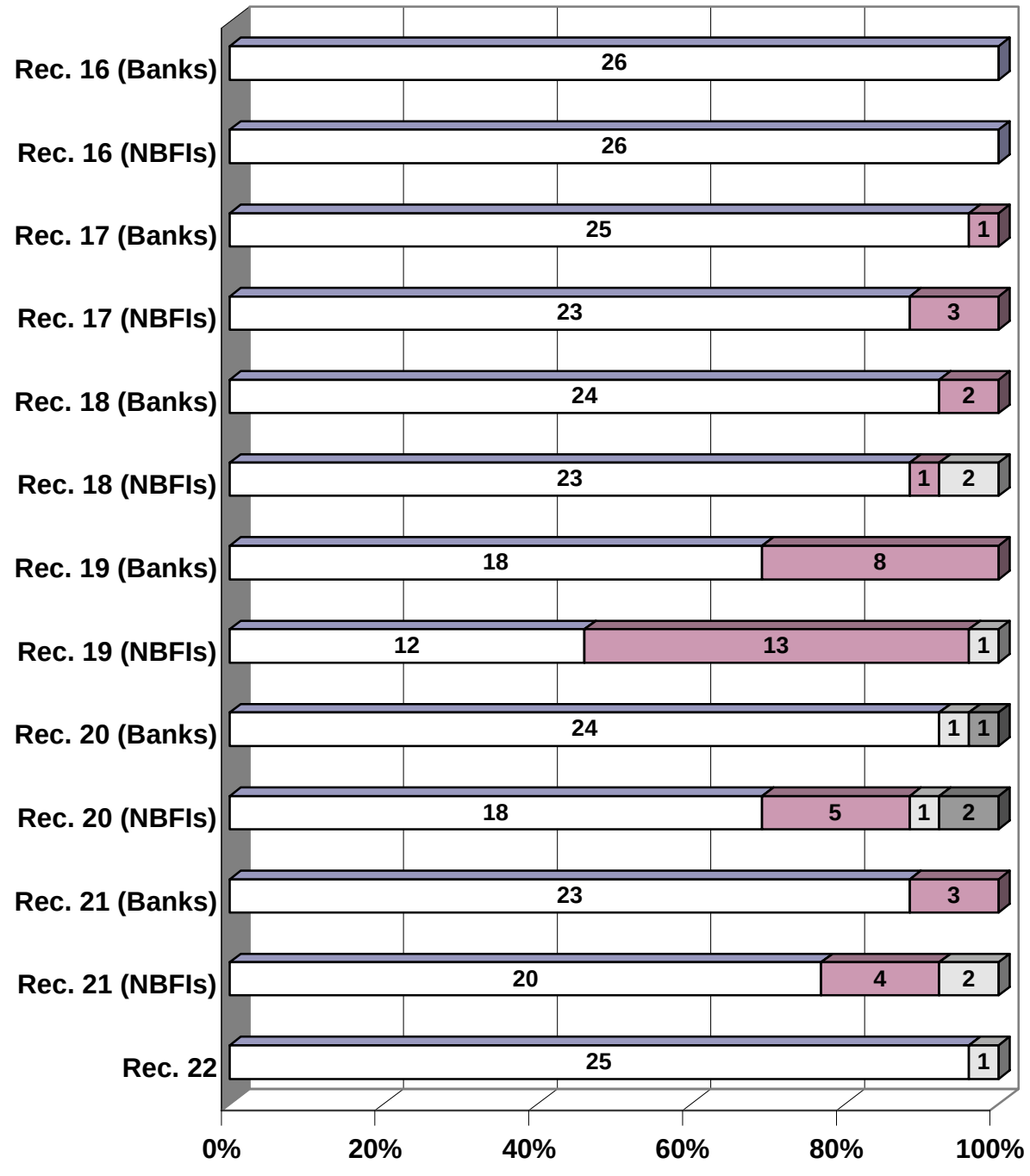
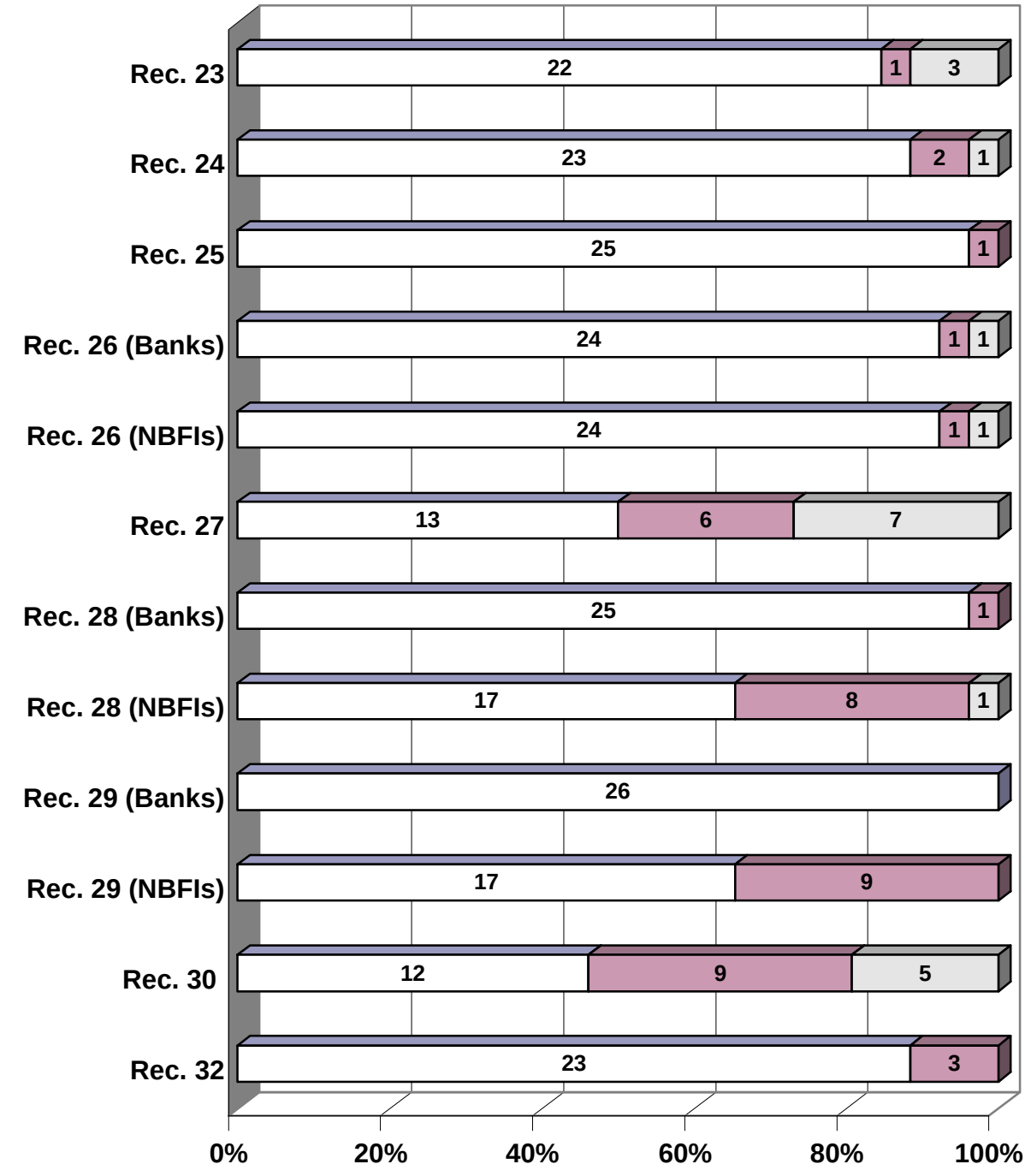


Chart 1 (c)

Compliance with the FATF 40 Recommendations
1998-1999 Self-Assessment Survey
— Financial Issues
(24 Recommendations — continued)



ANNEX C

FINANCIAL ACTION TASK FORCE ON MONEY LAUNDERING FATF

1998-1999 REPORT ON MONEY LAUNDERING TYPOLOGIES

10 February 1999

FINANCIAL ACTION TASK FORCE ON MONEY LAUNDERING 1998-1999 REPORT ON MONEY LAUNDERING TYPOLOGIES

I. INTRODUCTION

1. The group of experts met on 17-18 November 1998 under the chairmanship of Mr. Simon Goddard, Head of Intelligence, Strategic and Specialist Intelligence Branch, National Criminal Intelligence Service (NCIS). The meeting took place in the conference room of the European Bank for Reconstruction and Development (EBRD) in London. The group comprised representatives of the following FATF members: Australia, Austria, Belgium, Canada, Denmark, European Commission, Finland, France, Germany, Ireland, Italy, Japan, Luxembourg, the Netherlands, Norway, Portugal, Spain, Sweden, Switzerland, Turkey, the United Kingdom, and the United States. Experts from non-member international organisations with observer status, namely the Council of Europe, Interpol, the International Organisation of Securities Commissions (IOSCO), and the World Customs Organisation (WCO), also attended the meeting. The Council of Europe Select Committee of Experts on the Evaluation of Anti-Money Laundering Measures (PC-R-EV) was represented by Slovenia.

2. The purpose of the 1998-1999 typologies exercise was, as in previous years, to provide a forum for law enforcement and regulatory experts to discuss recent trends in the laundering of criminal proceeds, emerging threats, and effective countermeasures. While discussions of this exercise generally focus on money laundering developments within FATF member nations, the experts also attempt to examine available information on current money laundering patterns in non-member countries and other regions of the world. Prior to the meeting, delegations were invited to provide written submissions to serve as the starting point for discussions. In a departure from the format of earlier typologies exercises, this year's meeting was led off with in-depth presentations on a series of major money laundering issues that had been agreed upon during the FATF plenary meeting in September 1998.

3. The present report, therefore, focuses first of all on these major issues: the euro currency unit and large denomination banknotes, problems associated with offshore financial centres of non-cooperative countries or jurisdictions, challenges posed by new payment technologies, and the potential use of the gold market in money laundering operations. The report then continues with an examination of other money laundering trends in FATF countries followed by the overview of trends in non-member jurisdictions.

II MAJOR MONEY LAUNDERING ISSUES

(i) The single European currency and large denomination banknotes

4. The euro currency unit became the single currency of eleven European Union member states[20] on 1 January 1999. At that time, existing national currencies of the participating members became simply an expression of the euro. During the 'transitional' period that started on 1 January, the euro will not be issued in physical form; the participating members will continue to use their existing coins and notes. On 1 January 2002, euro coins and banknotes will be introduced, and, the existing national currencies of the participating members will then be withdrawn as legal currency by 30 June 2002 at the latest. The exact time for this final 'changeover' period (to occur between 1 January and 30 June 2002) will vary according to the implementing legislation of the individual participating member states.

[20] The eleven EU members involved in the introduction of the new currency include: Austria, Belgium, Finland, France, Germany, Ireland, Italy, Luxembourg, Netherlands, Portugal, and Spain.

a. Impact on Money Laundering

5. The primary period of potential risk is the six-month window during which the national currencies in paper and coin form will be exchanged for the euro. Some experts expressed the fear that money launderers might use this window to try to introduce illegally derived funds by hiding them among the expected higher volume of operations involving 'exchanges' of national currency for the euro. Other experts believed that there might be a rise in laundering in the time before the changeover — by using traditional methods, by exchanging these funds for currency from outside the euro zone, or by increased use of professional services providers — all to avoid detection during the actual changeover period.

6. With the elimination of 11 national currencies, it was agreed that the role of bureaux de change in the countries of the euro zone would diminish with regard to money laundering and its detection. Nevertheless, there could be an increase in exchange activities in those European countries outside the euro zone, especially involving traditional currencies such as US dollars, UK pounds, and Swiss francs. Moreover, once money has been converted to euros, the movement of these funds over national borders within the countries of the euro zone will cause less notice. One northern European country stated in its written submission that it might see an overall increase in the volume of cash in circulation prior to 1 January 2002 (with, for example, a possible influx of non-EU money — specifically Russian held US dollars — exchanged for euros).

7. The experts believed that there was little likelihood that international money launderers would convert national currencies to the currencies of non-participating countries (Danish or Swedish kroner, Greek drachma). The only exception, as mentioned above, is the UK pound, which will likely continue to be important in laundering related to certain types of narcotics activity. As for FATF countries in other areas of the world, the experts were of the opinion that the changeover to the euro would have little affect on laundering in North America, Asia or Australia, where the US dollar will probably continue to be the primary currency used in such activity. They recognised, however, that the euro used in wire or electronic transactions may turn up in money laundering operations anywhere in the world after 1 January 1999.

b. Impact on Anti-Money Laundering Measures

8. Almost all of the FATF member countries who are taking part in the changeover to the euro have started to pay attention to the specific money laundering concerns surrounding the introduction of the euro. The Netherlands, for example, has had a working group since 1996 to examine the problem and provide recommendations on necessary countermeasures. In Germany, the Federal Criminal Police produced a study in early 1998, which addresses the issue of the euro introduction as related to potential criminal activity. Italy has also set up a euro implementation co-ordinating committee of relevant ministries and authorities that will issue detailed implementation rules that take in to account the money laundering risks.

9. Many delegations felt that current anti-money laundering (preventive) systems should be adequate for detecting potential money laundering in this area. Since the changeover to the euro in banknote and coin form will require that national currency be physically presented at a financial institution, there was also felt to be a greater risk of detection for the launderer involved in such cash transactions. It was stressed that all member countries should continue to promote vigilance at financial institutions with regard to suspicious transaction reporting both prior to and during the changeover period.

10. The experts considered the possibility that the increased volume of all activity during the changeover period might overwhelm financial institutions personnel and might make them therefore more likely to miss or disregard potential indicators of money laundering. Another concern was related to which institutions actually perform the currency conversions. One FATF member country feared that

non-bank financial institutions involved in the changeover might not have adequate guidance on what constitutes suspicious activity regarding euro conversions.

11. A number of FATF members mentioned that they would increase awareness of the issue and reinforce anti-money laundering measures during the transition period. In the Netherlands, the potential problem with non-bank financial institutions is being dealt with by permitting only banks to carry out exchanges of national currency for euros. Germany will permit other financial services to perform these exchanges, however, only when these institutions are licensed to do so by the Federal Banking Supervisory Office (as is also required for operating a retail foreign exchange business). Additionally, the Federal Banking Supervisory Office issued new guidelines in March 1998 that lowers the threshold (whereby customer identification is required) to DEM 5,000 (USD 3,018) for conversion transactions.

12. Other issues brought up by the experts related to cross-border implications of the introduction of the euro both within and outside the countries of the euro zone. Italy mentioned that conversions of large amounts of national currency in other than its country of origin should be an indicator of suspicious activity. Similarly, conversions of large amounts of national currency to euros by individuals domiciled in other countries might also be a suspicious indicator. The United States raised the question of how existing national currencies (of the euro zone countries) held abroad will be exchanged for euros. These concerns highlight the fact that an internationally co-ordinated approach — relative to the introduction of the euro — still must be articulated for developing common money laundering indicators, specific sector guidelines, and sharing the information procedures among relevant national anti-money laundering services.

c. Introduction of the Large Denomination Euro Banknote

13. With the introduction of the euro in banknote and coin form (after 1 January 2002), the highest denomination banknotes will be EUR 500. This note will be roughly comparable in value to the highest denomination banknotes issued by Germany and the Netherlands. A number of FATF members have expressed concern that the issue of the high denomination euro banknote might make the currency more attractive to money launderers.

14. Several of the delegations saw the introduction of the large denomination euro as not only relating to the euro currency but also a potential problem in all countries having high denomination banknotes. Some of the countries of the euro zone already have high denomination notes (Austria, Belgium, Germany, the Netherlands), and the EUR 500 note was designed, according to the European Commission, to fulfil a similar role to that of the original national currency. Moreover, there are large denomination banknotes in other FATF member countries as well (Canada, Singapore, Switzerland), which may continue to exist after the introduction of the euro.

15. The legal use of large denomination notes is currently may often be concentrated in certain economic sectors (used automobiles, livestock, etc.) although this use could not account for all of the large denomination notes issued. Most delegations, including those from countries with large denomination banknotes, recognised that incomplete information is available on the legitimate use of these notes.

16. A number of FATF member countries have observed that large denomination notes tend to be used in the hoarding of money related to tax evasion or avoidance and in criminal activity. US cases illustrated how the bulk of small denomination currency and the difficulties involved in transporting it are still the primary obstacle for money launderers (and one of the easiest ways to detect them). As a further example of criminals preferring large denomination notes, Germany stated that kidnappers routinely demand that ransom money be provided in DEM 1,000 notes. In Canada, the CAD 1,000 bill was originally introduced to facilitate bank to bank transfers. This licit use has become outmoded with the ability of banks to transfer funds more rapidly and safely by electronic means. Criminal money

movements with these banknotes now show up almost exclusively as related to casino winnings. A case was cited in which CAD 70 million (nearly USD 45.7 million) in CAD 1,000 bills were alleged to have transited or still to be located in safety deposit boxes of a bank in central Europe.

17. Despite the fact that there is an incomplete understanding of the uses of large denomination banknotes in the legitimate economy, some of the experts felt strongly that the introduction of the EUR 500 banknote after 1 January 2002 may facilitate laundering. Other experts believed that large denominations may only facilitate movement of cash (whether legitimate or not) and not money laundering. Large denomination banknotes draw too much attention at financial institutions, thus presenting a potential launderer with increased risk of detection; therefore, 'middle-sized' denominations might be more suitable for the purpose of money laundering. Criminal proceeds denominated in EUR 500 banknotes would be considerably less bulky than the equivalent value of funds denominated in USD 100 bills. Current anti-money laundering measures within FATF members should be adequate for detecting suspicious cash transactions (including large denomination banknotes). However, with the expanded geographic region that comprises the euro area, there will be fewer internal points at which to detect suspicious currency shipments. It was therefore suggested that study of the subject should continue with a view toward clarifying the legal and illegal uses of large denominations.

18. In discussing the use of large denomination banknotes for laundering, and in particular the potential use of the EUR 500 note after 1 January 2002, the experts drew attention to the fact that the money laundering implications of the EUR 500 note do not appear to have been considered in planning for this large denomination banknote. The reason that the EUR 500 banknote was developed was to offer a denomination that would correspond with already existing high denomination banknotes in the countries of the euro zone. It was also noted by some of the experts that the use of high denomination notes in potential illegal activities, such as money laundering or tax evasion, was not taken into account. One delegation indicated that this issue had indeed been considered. Although experts mentioned a few economic activities in which the use of large denomination banknotes is especially common, the role of these denominations in legitimate commerce has apparently not been examined either. The majority of the FATF experts considered that the potential legitimate and illicit uses of large denomination banknotes ought to be thoroughly examined by the European Central Bank Furthermore, a number of the experts called for the FATF member countries to continue to study the subject with a view toward augmenting any other examination at the international level.

(ii) Offshore financial centres of non-cooperative countries or territories

19. During the past ten years, FATF member countries have made significant progress in adopting anti-money laundering regimes based on the standards set forth in the FATF Forty Recommendations. This progress has also been reflected in the increasing co-operation among members on anti-money laundering investigations. In non-member countries and jurisdictions, there have been signs more recently of an increased willingness to follow the FATF Forty Recommendations and co-operate on anti-money laundering investigations. This increased acceptance of FATF standards contrasts, however, with the unwillingness or outright refusal of certain important financial centres to co-operate in this area. The issue of non-cooperation was therefore identified by FATF members as one that should be addressed during the annual typologies exercise. The typologies discussions on the subject would then serve as a starting point for broader discussions on the issues of international co-operation. Prior to the experts meeting, FATF members were asked to examine the specific operational problems or difficulties that they had encountered with offshore financial centres in such areas as banking secrecy, shell companies, identification of beneficial owners, exchange of information, and other forms of international co-operation.

a. Impact on money laundering

20. Past typologies exercises began the task of identifying how 'offshore financial centres' facilitate money laundering. The experts at this meeting agreed that schemes involving these jurisdictions still appear to share common characteristics: a series of multiple financial transactions through the centre, use of nominees or other middlemen to manage these transactions, and an international network of shell companies (including a specialised 'off-the-shelf' variety that immediately go dormant upon completion of the series of transactions). Often an individual money laundering scheme will include more than one of these centres. An investigating agency can usually see the path that questionable funds follow into or out of such a scheme; however, the exact links between the funds and the illegal act that generated them are lost. Investigations of this type are often therefore unable to be fully exploited to a successful conviction or confiscation.

21. The oft-stated reason for creating an offshore financial centre has been to provide certain fiscal advantages to natural or legal persons that use its services. Since tax evasion schemes and money laundering operations often appear to use similar techniques, many money laundering experts believe that the quest for optimal 'fiscal advantages' is frequently used as a cover for moving to or through such locations what are in reality criminally derived moneys. One expert pointed out during this exercise, however, that there appears to be one significant difference between the techniques used for taking fiscal advantage of an offshore location and laundering criminal funds. In the former case, the funds usually move to a single offshore location where they are sheltered from the home country's fiscal oversight. In the latter case, that is, involving criminally generated funds, the tendency is for the funds to move rapidly through several offshore locations.

b. Impact on anti-money laundering measures: Role of the foreign legal entity

22. Virtually every FATF member represented at the experts meeting reported having experienced problems in pursuing anti-money laundering investigations with links to offshore financial centres. However, it was also pointed out that some offshore centres of non-cooperative countries were attempting to improve the level of judicial or investigative co-operation within the current framework of their national laws or by making selected changes to their legislation. The experts agreed, therefore, that the problem was most acute with those jurisdictions that are slow or unwilling to assist in international anti-money laundering investigations, particularly in regard to identifying the beneficial owners of legal entities.

23. FATF written submissions and a certain amount of discussion by the experts focused on the major problem posed by foreign legal entities to successful conduct of anti-money laundering investigations. Obtaining information from some offshore jurisdictions on the true owners or beneficiaries of foreign registered business entities — shell companies, international business companies, offshore trusts, etc. — appears to be the primary obstacle in investigating transnational laundering activity.

24. A number of FATF member countries mentioned that they regularly attempt to request information on foreign legal entities using mutual legal assistance treaties or other agreements with the offshore jurisdiction. Often non-cooperative jurisdictions refuse to respond to a foreign request for investigative or judicial assistance because there is no bilateral agreement that would permit such co-operation. The jurisdictions might also refuse the foreign request because the information requested is not maintained in any official registry. In some cases, information on legal entities may be protected from disclosure to foreign investigative agencies because of strict banking secrecy (with a variation related to non-release of fiscal information, including criminal or civil liability for disclosure) that is impenetrable even to domestic judicial or regulatory authorities. Some delegations also mentioned the increasing use of the Internet for the marketing and provision of such services.

25. The experts also highlighted the role of professional services providers in ensuring the good functioning of money laundering operations through non-cooperative jurisdictions. These solicitors, accountants, financial consultants, and company formation agents facilitate the creation of appropriate business entities that serve as the pipeline for moving funds of legal, as well as illegal, origin. Typically, such services are provided to non-residents of the jurisdiction and often at a higher level of confidentiality than that available to residents.

c. Potential solutions

26. In this regard, the experts hoped that the FATF ad hoc group on non-cooperative countries and territories, which was established in September 1998, would be able to develop strategies for addressing the issue. Several members pointed out that they are able to rely, in some cases, on existing international mechanisms for the exchange of information relating to money laundering investigations: mutual legal assistance treaties, memoranda of understanding, and Interpol. Nevertheless, these mechanisms do not work when the jurisdiction receiving the request for assistance refuses to honour it or does not maintain the desired information. The consensus of the experts was that every country or jurisdiction should have a mechanism in place for establishing the beneficial owners of legal entities registered within it and should have the authority to share this information with foreign counterpart investigative agencies. The development of internationally recognised minimum registration requirements would be welcome in this regard. Some of the written submissions also suggested that the so-called 'fiscal exemption' should no longer be valid grounds for refusing a foreign request. The work of the Egmont Group of Financial Intelligence Units (FIUs) was also mentioned as a potential channel for resolving this issue, given its work at the operational level to facilitate information sharing and the fact that many offshore financial centres already take part in its activities.

(iii) <u>New payment technologies</u>

27. All delegations continue to report that there have not been as of yet any investigated money laundering cases involving the new payment technologies identified in previous typologies reports. However, there have been several instances of other types of crimes — generally fraud schemes against unsuspecting members of the public — that have used the Internet as a means for committing the underlying offence. Law enforcement in FATF member countries remains concerned about the potential for use of these new technologies in money laundering schemes. Specifically, some of these risks include:

- inability to identify and authenticate parties that use the new technologies;
- level of transparency of the transaction;
- lack or inadequacy of audit trails, record keeping, or suspicious transaction reporting by the technology provider;
- use of higher levels of encryption (thus blocking out law enforcement access); and
- transactions that fall outside current legislative or regulatory definition.

a. Status of new payment technology systems

(l) Smartcards

28. Smartcards or electronic purses have been developed as an alternative to currency in paper and coin form. The electronic chip in the card can then store monetary value in electronic form which may then be spent as currency. Because the value on the card has already been debited from the financial institution, if the card is lost, there is no loss to the institution. There is thus no inherent reason for the financial institution to restrict the amount that may be held on an individual card

29. Smartcard systems in FATF member countries are mostly still in the prototype or early testing phases. Among these systems, there are many variants in terms of specific operating characteristics. Some of the systems are designed to provide transactional anonymity, while others capture data which may be used to construct an audit trail. In this regard, FATF members expressed some concern over the development of smartcard distribution through automated vending machines, which would allow virtually anonymous transfer of value to these cards. Within FATF member countries, the issuers/operators of many smartcard systems have placed limits on the amount of money that may be loaded onto the cards (for example, UK institutions have set the limits at GBP 50 - 500 [USD 82 - 820]); however, it was noted that this is not always the case. In one example, an institution in a non-FATF member country reportedly markets a smartcard with an upper limit of USD 92,000. Furthermore, while most smartcard systems do not permit so-called 'peer-to-peer'(direct 'card-to-card') transactions, others are developing the capability to move funds among card holders without recourse to a financial intermediary. In any case, it should be noted that, where there are limitations on card functions, these have been set by the card issuers and not by the respective national regulatory authorities.

(2) On-line banking

30. On-line banking has increasingly come to mean the method whereby certain types of financial transactions may be performed through the Internet website of those banks that offer this service. FATF members reported that there is a great deal of growth in this area. In the United States, nearly 85% of financial institutions have or are planning to establish such services. A significant number of financial institutions in other countries have also set up on-line facilities. In its most basic form, the service provided includes verification of cheque account balances and transfers among accounts at the same institution. In those systems that allow payments or transfers to be made, the customer is often restricted in the amount of transaction or the identity of the beneficiary. All of the systems require that on-line operations be tied to an already existing account at the institution; therefore, there is a continuous record of account activity.

31. The concerns mentioned in this area refer, again, primarily a lack of uniform regulation from supervisory authorities. Thus, although the customer's activity is tied to a particular account set up in his name, there is no way to verify the identity of the Internet transactor once the account has been opened. Indeed, if the on-line financial institution is located in an area known for high levels of banking secrecy and requires little or no proof of identity for opening an account, the money launderer could theoretically move funds from the convenience of his computer terminal. Although there were no reported cases of this type of laundering taking place at this time, the experts believed that technology was developing rapidly and thus worthy of further vigilance.

(3) E-Cash

32. Electronic cash (or 'e-cash') seeks to provide a way of paying for goods and services across the Internet. In concept, e-cash would replace notes and coins for normal Internet transactions; however, it has the added advantage of being able to be split into fractions of the lowest denomination coins to allow what are termed 'micropayments'. These small payments could be made for reading specified sections of on-line newspapers, for example. Under most existing payment systems, these micropayment transactions would not be economical. With e-cash, the customer buys value from an authorised provider — as with the smart card — however, the value is then stored either in customer's home computer or a safe repository on-line. When the funds are spent, the e-cash value is credited to a retailer's e-cash account that then must be later 'up-loaded' to the retailer's regular bank account. Security of e-cash systems is concerned primarily with ensuring that value cannot be created except by authorised institutions or that the same value cannot be spent more than one time.

33. Concerns with regard to e-cash are generally the same as those mentioned for smart cards. Since only the initial purchase and the final settlement stages take place through banks, the risk exists that there will be no way to track e-cash in transactions taking place after the initial purchase and before final crediting of the value to a retailer's account. Some systems currently being tested have set limits to the amount that an e-cash 'purse' may hold; however, there is at present no uniform regulatory standard, and it is not certain that such regulations would do much to limit the use of e-cash by the consumer. The anonymity of e-cash, similar to coin and banknotes, may also hinder the financial institution with reporting obligations from positively identifying the ultimate source of an e-cash transaction. A further concern is that currently available computer encryption systems may further shield e-cash transactions from the scrutiny of investigative authorities.

b. Countermeasures

34. Smart cards appear to be able to replicate all of the functions of e-cash while allowing portability and use in the real world, as well as over the Internet. There was some uncertainty expressed, therefore, over the ultimate success of e-cash systems. Nevertheless, the experts agreed that the field of new payment technologies is changing very rapidly, and that developments in e-cash systems, along with those of the other proposed systems, should continue to be monitored. The experts discussed a number of possible measures that might limit the vulnerability to money laundering on the new payment technologies. These measures included the following:

- limiting the functions and capacity of smart cards (including maximum value and turnover limits, as well as number of smart cards per customer);
- linking new payment technology to financial institutions and bank accounts;
- requiring standard record keeping procedures for these systems to enable the examination, documentation, and seizure of relevant records by investigating authorities; and
- establishing international standards for these measures.

(iv) Potential use of the gold market in money laundering operations

a. General

35. Following last year's introduction to the issue of money laundering through the gold market, the FATF experts were asked to provide specific examples of such cases from their national experience. A number of members did provide example of cases in which gold transactions were an integral aspect of the investigated money laundering scheme. These cases involved the purchase of gold with illegally obtained funds. The gold was then exported to other locations where it was sold, these funds thus being legitimised as the proceeds of gold sales. Existing reporting requirements for gold purchases were circumvented by structuring the purchases to amounts below the reporting threshold.

36. Several members reported that the vulnerability to money laundering within their countries has increasingly centred on specialised gold bullion sellers. This is due in part to the fact that anti-money laundering legislation targeting traditional financial institutions has generally caused those customers desiring to purchase bullion anonymously to turn to other sources. In many FATF member countries, there is no suspicious transaction reporting requirement directed toward bullion dealers or other non-financial banking institutions dealing in gold. Additionally, even though the import or export of gold bullion seems to be a key part of money laundering schemes involving the material, members reported that the lack of import / export reporting requirements appears to hamper detection of illegal operations.

37. Members were in some cases able to identify cities or regions within their jurisdictions that specialise in legitimate gold business (for example, Cordobá in Spain and Arezzo and Vicenza in Italy) or in which significant business takes place (Paris region and Marseilles in France). Gold purchases in these areas are often conducted in cash and frequently in non-indigenous currency (especially US dollars). Gold serves as both a commodity and, to a lesser extent, a medium of exchange in money laundering conducted between Latin America, the United States and Europe. In this cycle, gold bullion makes its way to Italy via Swiss brokers. There, it is made into jewellery, much of which is then shipped to Latin America. In Latin America, this jewellery (or the raw gold from which it was made) then becomes one of, if not the most important commodities (others include various consumer goods and electronic equipment) in the black market peso exchange money laundering scheme.

38. Several FATF members also mentioned having received suspicious transaction reports involving gold transactions. In some instances, these transactions appeared to reflect attempts to avoid high VAT rates by making large purchases of gold in countries with low VAT rates and then exporting the bullion back to the country of origin where it could then be resold at a profit.

b. Hawala / Hundi alternative remittance system and gold

39. The question of laundering through the use of gold as a commodity and as a medium of exchange was discussed by the experts in the context of the hawala / hundi alternative remittance system. The word 'hawala' means 'trust' or 'exchange'; 'hundi' means 'bill of exchange'. It is an alternative remittance system that enables the transfer of funds without their actual physical movement (often without the use of a traditional financial institution). Very often, using hawala is more cost effective and less bureaucratic than moving funds through officially recognised banking systems. Built on a system of trust and close business contacts, hawala originated in South Asia; however, it is now used as an alternate remittance system throughout the world.

40. In the laundering associated with this system, gold often plays the role of the primary medium of exchange in certain transactions. Although many hawala transactions may take place without gold, many of these transactions involving the movement of money to South Asia often do involve the metal. There are two reasons for this: the first is the combined historical, religious and cultural importance that gold enjoys in the region, and the second is the increasing distrust in the value of local currencies (many South Asian nations prohibit speculation on their currencies, and exchange rates are fixed by the central banks). World-wide, gold is often used as a hedge against inflation; in South Asia, gold is often the primary means of preserving and protecting wealth.

41. In one scenario, a gold dealer operating in one country also operates as the 'banker' for various jewellery shops in his region. These jewellery shops give him the cheques and cash they receive for purchases; he processes these through his own bank accounts. In return, he furnishes them with scrap gold and gold jewellery for use in their businesses. He retains a few percentage points of the money he receives from them for his 'services' (as well as for the legal risk he is incurring). The owners of the jewellery shops do not have to deal with the bureaucracy of banking, and, since there is almost no paper trail of their sales, they enjoy a greatly reduced tax liability.

42. In another scenario, money may be moved from one country to another through the hawala system. A 'hawaladar' (hawala broker) based in one country facilitates this movement by receiving payments in the local currency. He then makes contact with a hawaladar in South Asia and instructs him to make the necessary payment to a specified beneficiary in that local currency. In order to settle his accounts with the South Asian hawaladars, the hawaladar in the first country might send postal money orders or some other financial instruments to a precious metals house in the Persian Gulf. This precious metals house then effects payment to the South Asian hawaladar in gold (either into a safe-keeping account under his name or by direct export of the gold to the South Asian location).

III. MONEY LAUNDERING TRENDS IN FATF COUNTRIES

(i) Sources of illegal funds

43. Narcotics trafficking appears still to be the primary single source of criminal proceeds among the majority of FATF members. The various types of fraud (fiscal, EU funds, value added tax, insurance, bankruptcy, etc.) are the next major source of illegal funds, if not, in some jurisdictions, the primary source. Organised crime activity generates a considerable amount of illegal proceeds that are laundered in or through FATF member countries. Some members have noted with concern the increasing trend for these crime groups to operate in loose alliances (Russian and Latin American groups, for example). Written submissions from some of the members also mentioned an increase in the number of cases in which laundering was related to official corruption or the funding of international terrorism.

44. The United States has recently substantially elevated the priority assigned to combating terrorist financing (which can constitute the crime of money laundering in the United States). In October 1997, the US government designated 30 foreign organisations as foreign terrorist organisations. In June 1998, US federal authorities seized USD 1.4 million in cash and property held by individuals and an organisation whose funds were reportedly part of a scheme to support Middle Eastern terrorism. The funds were transferred by wire from Europe and the Middle East to financial institutions in the United States and, through various means, were then used to facilitate recruitment, training, and operations of the terrorist group Hamas. This case marks the first time that civil asset forfeiture laws were used in the United States to seize assets suspected of being involved in money laundering violations related to foreign terrorism. These terrorist operations included a conspiracy to commit extortion, kidnapping, and murder against the citizens and the government of Israel.

(ii) New or significant trends

a. General

45. Many of the submissions of FATF member countries noted an increase in suspicious transaction reporting, both for certain individual money laundering methods and in overall numbers of reports. As for new methods, however, with the exception of new payment technologies described above, the submissions appear to indicate that launderers are using the same practices that they have done in the past. Money laundering within FATF members is characterised, therefore, by a finite number of techniques that can be combined into an almost infinite variety of laundering schemes. Laundering activity is also characterised by its ability to change quickly when faced with new countermeasures by shifting to other techniques or mechanisms, combining these methods into new schemes, or by moving to sectors or regions where government oversight represents less of a threat.

46. Indeed, this last point was cited by virtually all members as a fundamental truth of money laundering today: the lack of comprehensive preventive measures in a particular sector or region will inevitably attract money laundering activity. Members continue to mention bureaux de change, money remittance businesses, and casinos as particularly vulnerable to laundering in some locations. Often these are combined with cash smuggling, alternate remittance systems, or the use of offshore registered businesses, all of which generally operate beyond the framework of traditional financial oversight systems.

47. Another particularly evident trend in the money laundering schemes described by the FATF experts is the growing role played by professional services providers. Accountants, solicitors, and company formation agents turn up ever more frequently in anti-money laundering investigations. In establishing and administering the foreign legal entities which conceal money laundering schemes, it is these professionals that increasingly provide the apparent sophistication and extra layer of respectability to some laundering operations. These services are offered not only at offshore locations (as described above) but also within FATF member countries. One delegation described a money laundering scheme in which a criminal group selected a firm of solicitors to act on their behalf in the purchase of a company. The funds for the purchase were delivered to the solicitors in cash and placed in a client account. When the purchase later fell through, the funds were returned — less fees — to the criminal group in form of a cheque. In fact, the group already owned the company they were attempting to 'buy' and had arranged for the failure of the sale since they only wished to convert their criminal proceeds into a cheque from a respectable law firm. This scheme was revealed in a suspicious transaction report from the law firm concerned. More often than not, however, professional services providers are still not subject to suspicious transaction reporting requirements in FATF members. Even when they are subject to such a requirement, the numbers of disclosures made to authorities are frequently disappointing.

48. Even in instances where preventive measures have been implemented, laundering activity still occurs, according to the FATF experts. When faced with suspicious transaction reporting at both banks and other financial services, launderers frequently resort to structured transactions to avoid the reporting threshold. Despite border controls designed to detect smuggling of cash criminal proceeds, bulk shipments of cash continue to be observed by FATF members. The use of legitimate appearing business transactions — claiming that proceeds are generated by a legal currency exchange business, the profit from bona fide commodity sales, the result of factoring operations, for example — is a standard cover used by launderers to hide the criminal origin of those funds. Members mentioned that the only indicator of money laundering in these cases is often the disproportionate size of the transactions (either individually or in aggregate) when compared to the expected economic activity of the business.

49. Several FATF members reported an increase in the appearance of insurance products in laundering schemes. Various products have been noted, including life and property insurance and long term capitalisation bonds. Launderers generally pay for the insurance using the cash criminal proceeds. They then request early pay out of the policy (in the case of life insurance or capitalisation products) or make a claim against the property insurance, thus obtaining a 'legitimate' insurance refund or claim payment.

50. Electronic funds transfers continue to be the preferred method for the layering of criminal proceeds once they enter the legitimate financial system. Frequently, these proceeds are smuggled out of the FATF member country, deposited into the financial system at a foreign location, and then wired back to the country of origin. Wire transfers are often associated with foreign registered business entities as described above. If criminal proceeds are transmitted through 'transit' accounts set up in offshore financial centres or — as have been found in some FATF member countries according to the written submissions — the beneficial owner of the funds is effectively hidden.

b. Derivatives and securities markets

51. In recent FATF meetings, questions have arisen concerning the perceived vulnerabilities of the derivatives and security markets as a vehicle for money laundering. As part of the written submission of one member, a paper was prepared on this issue and provided to the experts. According to the paper, there is good reason to suspect that money laundering may pose a substantial threat in these markets. Compared to banks, the derivatives markets and associated products represent perhaps a better opportunity for laundering because of the ease with which audit trails can be obscured. Indeed, any product that offers rapid commercial decision making, high speed transfer, obscurity of control, or complication of audit trail is at risk. Operators in these markets, when compared to banks, tend to be less

familiar with anti-money laundering efforts. There is also evidence — a good example is the BCCI case — which shows the readiness of criminals to use financial products for laundering.

52. The primary opportunity for laundering is in the complex derivatives market. Derivatives are securities that derive their value from another underlying financial instrument or asset; they have no intrinsic value of their own. There are three primary types of derivative contracts: forward contracts, futures, and options. All of these instruments, in simple terms, are contracts sold as a hedge against the future risk of fluctuations in commodity prices, time differentials, interest rates, tax rates, foreign exchange rates, etc. Because of the flexible nature of these products, the derivatives market is particularly attractive to operators willing to risk heavy losses. A high volume of activity on the market is essential to ensure the high degree of liquidity for which these markets are known. The way in which derivatives are traded and the number of operators in the market mean that there is the potential obscuring of the connection between each new participant and the original trade. No single link in the series of transactions will likely know the identity of the person beyond the one with whom he is directly dealing.

53. The derivatives markets have traditionally not been subject to strict regulatory oversight under the assumption that its operators, as high risk investors, do not need the same level of protection. The introduction of stricter controls would necessarily cause investors to look elsewhere for these markets. For fear of scaring of investors, there is thus no incentive for traders on the market to ask too many questions. This lack of rigorous government control makes the derivatives market even more attractive from the perspective of a money launderer.

(iii) New countermeasures implemented or significant modifications to existing measures

54. The level or type of money laundering activity can change rapidly in response to countermeasures implemented by a particular jurisdiction. FATF members continue to re-examine their anti-money laundering efforts and refine them where necessary. Faced with difficulties in prosecuting money laundering under provisions dealing with receipt of stolen goods, Sweden and the Netherlands plan to set up separate offences of money laundering under their respective penal codes. Some FATF members have extended the list of predicate offences for laundering or plan to do so.

55. Several FATF member countries are working to extend preventive measure (suspicious transaction reporting) beyond the traditional banking sector. New Belgian legislation this year, for example, extends suspicious transaction reporting (STR) requirements to real estate agents, bailiffs (‘huissiers de justice’), money courier services, notaries, accountants, and casinos. Sweden plans to introduce a reporting requirement on money laundering for external auditors.

56. The Netherlands has introduced legislation which requires money transfer businesses to report unusual transactions. Germany has already placed a requirement on such businesses to obtain a licence from the Federal Banking Supervisory Office (FBSO), the same authority that oversees banking activity. Additionally, the FBSO requires that all transactions dealing in foreign currency valued at DEM 5,000 (USD 3,018) require customer identification. Finland has extended suspicious transaction reporting to its entire financial sector, includes casinos and other gambling related businesses, and has consolidated reporting to a single financial intelligence unit. Similarly, Switzerland’s reinforced money laundering legislation, which also establishes a centralised reporting unit, came into effect in April 1998. This legislation also extends the suspicious transaction reporting obligation to all financial sectors.

57. Japan plans to enact legislation that will strengthen its measures for combating money laundering and organised crime, and this legislation is currently under deliberation in the Diet. This legislation will extend the number of predicate offences for money laundering, provide for enlargement of the measures

for confiscation and freezing the proceeds of crime, and centralisation of suspicious transaction reporting under the Financial Supervisory Agency.

58. Canada is working to amend existing legislation to require mandatory reporting of suspicious transactions, as well as cross border movement of currencies. The amendment will clarify the ambiguity surrounding the definition of suspicious transactions and when they are required to be reported. Legislation permitting law enforcement to conduct money laundering sting operations has already been implemented.

59. It has become clear that the analysis and discussion of trends in virtually all FATF member countries now begins with analysis of suspicious transaction reports. Preventive systems involving these reports, implemented and used widely to help detect individual instances of money laundering, are the starting point for examining the money laundering phenomenon from a more strategic point of view. This is reflective of the increase in the number of FATF member states which now have functioning financial intelligence units (FIUs) and mandatory suspicious transaction reporting regimes. The written submissions of the experts, as well as the discussions during the typologies meeting indicated that suspicious transaction reporting systems are becoming more effective in detecting new money laundering methods. The ability of FIUs to share information, even informally, has also dramatically increased.

IV. MONEY LAUNDERING TRENDS OUTSIDE FATF COUNTRIES

60. Money laundering is a problem that is not restricted to FATF members alone. Countermeasures implemented in FATF member countries have facilitated the collection and analysis of information on money laundering activity within their respective national areas. These countermeasures have also, in some cases, pushed certain money laundering activity to jurisdictions having little or no anti-money laundering regime. At the same time, an increasing number of non-FATF countries have established or are in the process of developing effective money laundering countermeasures. Nevertheless, information provided by the FATF experts on non-member countries is far from complete; therefore, the following assessment of money laundering trends outside the FATF member countries does not claim to be exhaustive.

(i) Asia and the Pacific Region

61. Sources of information on money laundering activities in the region have been limited. While few non-FATF members in the area have implemented comprehensive anti-money laundering programmes, there have been some signs that individual countries are moving to establish such systems. Some FATF members nevertheless continue to find evidence of significant money laundering activity or serious vulnerabilities to it.

62. As noted in previous typologies exercises, South Asia continues to be one locus in the region for such activity. It serves as home to several major international banks and is a transhipment point for drugs produced in Afghanistan and Iran to the west and in Myanmar, Thailand, and Laos to the east. Money laundering related to the narcotics trade, financial fraud, corruption, and other activities is believed to be carried out through both the traditional banking system and the hawala / hundi alternative remittance system.

63. In the Pacific region, a heavy concentration of financial activity related to Russian organised crime has been observed, specifically in Western Samoa, Nauru, Vanuatu, and the Cook Islands. One delegation mentioned an increasingly common scheme whereby apparently American middlemen are used to open accounts or charter banks in one of the locations. Given the increased suspicion aroused by visible Russian business activity in these jurisdictions, the laundering scheme thus operates under the

cover of non-Russian linked business. Internet gambling, which generates nearly $1.5 million a month in this region, represents a major new business trend in Western Samoa, Niue, Vanuatu, Tonga, and Fiji and another potential vulnerability for money laundering and financial crime in those jurisdictions.

64. FATF members greatly welcomed the fact that the Asia/Pacific Group (APG), this region's new anti-money laundering body, held its first typologies workshop in October 1998 in Wellington, New Zealand. Experts from 25 jurisdictions in the area and 4 international organisations met for two days to highlight the most significant money laundering issues of their particular jurisdictions, as well as the Asia/Pacific region as a whole. The Asia/Pacific Group had not yet released its final typologies report by the time of the FATF experts meeting; however, the group provided a short submission to the FATF which described some of the key findings of the APG experts.

65. The primary sources of criminal proceeds in the region were identified as trafficking in human beings and illicit drugs, gambling and the activities of organised crime groups. Some other identified sources include kidnapping, arms smuggling, hijacking, extortion, public corruption, terrorism and tax evasion. It was also noted that the perpetrators of the predicate offences commonly launder their own proceeds.

66. Among some of the methods employed for laundering, the APG experts cited the abuse of offshore financial centres and the increasing presence of solicitors, accountants, and other professionals both to set up business entities and facilitate the administration of accounts used in money laundering. Structured transactions, purchase of monetary instruments (bank drafts, cheques), and physical removal of currency or monetary instruments were also observed in the region. Criminal proceeds have been moved through the Asia/Pacific area by traditional (electronic) means, as well as alternative remittance systems. The APG experts also mentioned that criminal proceeds are often transferred out of the region under the guise of real estate or other investments, legitimate gambling proceeds, and through the use of credit and debit cards. The group expressed similar concerns to those mentioned by the FATF members regarding the development of new payment technologies.

67. FATF members welcomed the APG decision to hold an annual typologies workshop and noted that the second APG workshop will be held in Tokyo, Japan, on 2-3 March 1999. The workshop will concentrate on the use of underground banking and alternative remittance systems for money laundering purposes.

(ii) Central America, South America, and the Caribbean Basin

68. Drug trafficking and the money laundering activity it engenders continue to be major problems in this region. While most of the countries of the Western Hemisphere have moved to enact anti-money laundering legislation, a number of jurisdictions have not fully implemented these countermeasures. Potential alliances between the region's narcotics traffickers and Russian organised crime, already detected by some FATF members, are a cause for concern, as they may further expand money laundering connections with Europe, North America, and the Pacific regions.

69. With regard to the Caribbean area, the Caribbean Financial Action Task Force (CFATF) completed the last phases of its typologies exercise. The exercise comprised four parts conducted over a two-year period. As mentioned in last year's report, the first two phases of its exercise — examining laundering activities in domestic financial institutions and through the gambling industry — took place during 1997. Since then, CFATF has undertaken an assessment of laundering as it occurs in international financial transactions conducted in both domestic and offshore financial institutions, and also the emerging cyberspace technologies. It is most encouraging to see that CFATF will organise a typologies conference on the vulnerabilities of free trade zones to money laundering activity. CFATF plans to use

the conference, which will be held in Port of Spain during March 2000, to develop a model free zone compliance programme and code of conduct.

70. Money laundering activity in the Caribbean region remains a significant problem due to its location near major narcotics production and consumption areas and its concentration of offshore financial centres. Antigua was again cited as particularly vulnerable due to its failure to implement fully its existing anti-money laundering legislation. Free trade zones were also mentioned as continuing targets for money laundering schemes. In one instance, wire transfers have increasingly replaced cash deposits as the means of moving illegal proceeds through the jurisdiction. St. Kitts was mentioned as being of some concern due to a reported increase in narcotics related laundering activity. Suspicious transactions have been detected within French overseas departments in the Caribbean area relating to structured deposits.

71. The laundering of criminal proceeds continues to affect the many other nations of Latin America. Narcotics trafficking remains the primary source of these proceeds. Despite steps taken by the Mexican government in the past year to address the problem, laundering activity is still of serious concern in that country. Cross-border laundering of drug proceeds between the United States and Mexico continues with currency smuggling, use of payable through accounts, bureaux de change and the black market peso exchange identified as the key laundering methods. Mexican drug cartels remain the primary force in this activity, although the Colombians still play a role. These organisations are able to operate in Mexico by taking advantage of loopholes in existing legislation. Corruption continues to hamper the country's anti-money laundering efforts.

72. Costa Rica was mentioned in connection to laundering activity through financial institutions, casinos, bureaux de change, bulk currency smuggling, and real estate investments. As reported last year, Colombia continues to see the black market peso exchange being used as the primary money laundering system by narcotics traffickers based in that country. The rising cocaine demand in Europe has reportedly resulted in an increase in funds needing to be laundered in the area and the formation of new alliances between Colombian narcotics traffickers and Russian organised crime groups.

73. With its role as a major finance and trading centre and its proximity to Colombia, Panama remains attractive to money laundering schemes. The Colón Free Zone is a key target for these laundering activities despite the extension of anti-money laundering measures to the area. Suriname is another country of the region that has an increasingly visible money laundering problem. Methods detected in that country include over-invoicing, gold purchases and account manipulation. Recently, high-level Surinamese officials have been implicated in laundering activity related to international narcotics trafficking.

(iii) Central and Eastern Europe

74. The countries of Central and Eastern Europe remain a significant concern to FATF members. Illegal proceeds are generated by contract and privatisation fraud schemes, as well as from the extraction and production of natural resources. In Central Europe, financial institutions continue to be victims of fraud schemes using misrepresented collateral and carried out with the collusion of bank officials. Embezzlement of corporate funds through false contracts is also still a problem.

75. Organised crime activity operating out of the former Soviet Union area was mentioned as being of continuing concern. Many of these organised crime groups bring their criminal proceeds to the nearby FATF members in Europe where they make large real estate investments in such areas as the French and Spanish Mediterranean coast. The groups frequently transfer their funds through various offshore financial centres, such as the Channel Islands, Gibraltar, and the Caribbean area, before using the funds

for these investments. The transfers are sometimes made in the name of a legitimate appearing business entity registered in an FATF member country; however, upon further investigation, it is found that the company has no place of business or bank account in the country of registry.

76. FATF members also noted their concern over potential connections of financial institutions to Eastern European organised crime. It is difficult to determine the exact role that Russian financial institutions may wittingly or unwittlingly play with regard to organised crime activity. This difficulty extends to Russian business entities, as well. One member noted that banks operating in Europe seem to be less critical when dealing with other banks even if the counterpart is Russian.

77. A number of members noted an increase in the number of couriers of Central or Eastern European origin involved in reports of unusual or suspicious transactions. These transactions seem especially prevalent with regard to operations at bureaux de change located in FATF member countries. The couriers have no known business or residence connections in the country where they attempt to conduct single transactions with relatively large amounts of cash (individual transactions range from USD 50,000 to USD 100,000). The large sums and the manner in which the transactions occur seem to indicate that these individuals are not simple tourists.

78. Central and Eastern Europe countries have made a certain amount of progress in developing, adopting and implementing countermeasures during past year. Some examples of this progress include the following: Bulgaria, Estonia, Latvia, Lithuania, and Romania have all enacted anti-money legislation. Latvia and Lithuania have operational financial intelligence units, and Poland hopes to have an operational unit in the first part of 1999. Despite its many internal problems, Russia has enacted a new criminal code that includes money laundering as a crime. The Russian anti-money laundering legislation is scheduled to be approved by the country's parliament in early 1999. Ukraine has effectively abolished anonymous accounts, and its Ministry of Justice is in the process of drafting its first comprehensive anti-money laundering laws. Nevertheless, some FATF members noted that it is still often difficult to obtain information relating to anti-money laundering investigations from certain of the countries of the region. One member mentioned that many of the Central and Eastern European countries have experienced similar frustrations in attempting to obtain information on foreign registered business entities from offshore financial centres in support of their anti-money laundering investigations.

79. FATF welcomed the further development of the Council of Europe initiative to evaluate anti-money laundering systems. The select committee set up for this purpose has adopted an evaluation process based on the one used by the FATF. Its goal is to evaluate the countermeasures in place in each of the 21 members of the committee (the non-FATF members of the Council of Europe). During 1998, the committee conducted seven mutual evaluations. The committee also held its first typologies exercise in December 1998, and it is hoped that this will become a recurring event. Indeed, the Council of Europe typologies exercise, along with those of APG, CFATF, and the FATF, should become the basis for a much clearer picture of money laundering activities throughout the world.

(vi) Middle East and Africa

80. Information on laundering activities in this area of the world is extremely limited. A number of factors favourable to money laundering are known to be present throughout both regions. In the Gulf States (particularly in Bahrain), the banking and finance industries are well established on an international scale. Only a few of the jurisdictions of the region have anti-money laundering legislation. Many expatriate labourers working in the region regularly send money home by using the traditional hawala / hundi alternate remittance system, which offers more favourable rates than those of traditional banks. Gold smuggling is also reportedly used — especially by some professional criminal organisations — as a

means of moving funds through the Gulf into the South Asian region. Free trade zones of the area are also likely to attract some of this laundering activity.

81. Still less is known about the Mediterranean area. The growing presence of its own financial centres and its role as a drug transit area appear to make the region vulnerable to laundering activity. Such activity involving organised crime and the diamond industry in Israel has been observed by some FATF experts. With only a few exceptions, most jurisdictions of the region are characterised by the total absence of comprehensive anti-money laundering programmes.

82. Africa south of the Sahara is also considered by many of the FATF experts to be vulnerable to money laundering, although, again, information on the region is limited. A factor which contribute to this vulnerability is the increasingly widespread activity of indigenous and, to certain extent, non-indigenous organised crime groups. These groups can operate throughout the region due to lack of strong anti-money laundering laws, combined with the endemic corruption, lack of training, and low pay of government authorities. Only South Africa has criminalised money laundering for crimes beyond those related to narcotics trafficking; however, it has yet to enact comprehensive preventive measures. In other countries of the region, it is believed that only about 20% of the population use traditional banks; thus, there is some concern about how preventive measures could be applied there.

83. FATF experts noted again the ubiquity of West African (especially Nigerian) organised crime groups in money laundering schemes that link FATF countries with the region. As noted in previous reports, fraud seems to be one of the most pervasive sources for laundered funds; however, these groups are also involved in narcotics trafficking, arms smuggling, auto theft, gemstone and ivory smuggling, and trafficking in stolen identity documents. One member noted that there were increasingly ties with some of the francophone countries of western Africa, particularly Togo, Benin, and Senegal. In general, there appears to be a growing frequency of using bureaux de change operations as a cover for converting criminal proceeds. Some groups are using bank accounts in FATF member countries as collector accounts for these proceeds. Funds from these accounts are then used for the purchase of goods that are shipped to Africa and sold as 'legitimate' imports. The holders of these accounts charge a percentage for their use but otherwise have neither interest in the source of the funds nor any direct link to the transactions.

V. CONCLUSIONS

84. The London meeting of the group of experts on typologies in November 1998 was the second to undertake in-depth discussions on more focused topics. As mentioned last year and as evidenced by the written submissions of the FATF delegations, the basic techniques and mechanisms for money laundering have been well documented. This meeting examined a number of areas that had not been fully developed. It is hoped, therefore, that the purpose of these expert meetings will continue to be the identification of new approaches taken by launderers, along with significant changes in the patterns of their activity. Through this work, the FATF will acquire additional support and, one might hope, new ideas for appropriate laundering countermeasures.

85. With regard to the money laundering implications of the introduction of the euro in the eleven members of the Economic Monetary Union, experts agreed that there was a potential risk of overwhelming of existing preventive measures due to the increased burden of work for financial institution personnel during the transition phase. The experts also agreed that the introduction of the euro would be a possible opportunity to detect laundering activity. The critical time as far as risk is concerned is the period from January to June 2002, when euros in coin and paper form will replace national currencies. Existing preventive countermeasures should be adequate in detecting possible laundering activity, although a number of FATF members are taking extra steps to re-emphasise or reinforce their anti-money laundering programmes. Some experts believe that the introduction of the large denomination

euro banknote (EUR 500) after 1 January 2002 could affect laundering activity by reducing the bulkiness of criminal proceeds when transported.

86. Non-cooperative jurisdictions or territories remain a continuing area of concern to FATF members. The inability to obtain relevant information on the beneficial owners of foreign legal entities — shell companies, international business corporations, offshore trusts, etc. — represents one of the major roadblocks to successfully detecting, investigating and prosecuting suspected international money launderers. There is the need to foster increased awareness of this problem and exert pressure on certain offshore financial centres in international fora where appropriate. The efforts of the FATF ad hoc working group on non-cooperative countries — both FATF and non-FATF members — will be most welcome in this area.

87. Rapid development and growing consumer acceptance of smartcards, on-line banking, and e-cash continue to be the hallmark of these new payment technologies. As recently as two years ago, many of these systems were not yet beyond the prototype stage, and the potential implications on laundering activity were seen as theoretical. Smartcards are beginning to move beyond testing, and on-line banking is already a reality in a few FATF member countries (and potentially available world-wide through the Internet). The abuse of these systems by launderers is no longer a distant possibility. FATF experts noted that certain money laundering countermeasures could be easily added to the systems; however, decisions to do so have been left to the system developers. Without consistent standards and appropriate regulatory oversight, these new payment technologies will remain highly vulnerable to money laundering activity.

88. Awareness of the potential role of the gold market — and, by extension, of other high-value commodities markets — is growing among FATF member countries. Transactions involving gold are increasingly found in money laundering schemes and are often an integral part of money movements through various parallel banking systems, such as the hawala / hundi system discussed during this typologies meeting. It was emphasised that these money laundering schemes are not limited to any single region of the world. Nevertheless, the particular focal point of gold dealers in the Gulf States for hawala / hundi money movements to and from the South Asia region should be noted.

89. The experts noted the apparent increasing trend for professional services providers — accountants, solicitors, company formation agents, and other similar professions — to be associated with more complex laundering operations. These professionals set up and often run the legal entities that lend the high degree of sophistication and additional layers of respectability to such money laundering schemes. Operating not only in certain offshore locations where they are protected behind a wall of strict confidentiality, these professionals sometimes also provide similar services within FATF member countries themselves. Currently, only a few FATF members impose an obligation on professional services providers to report suspicious transactions. Those members that do have this requirement are not always satisfied with the amount of reporting that takes place from this sector, although the quality of individual reports in some cases appears to justify the need for such reporting.

90. Lastly, this meeting of experts on money laundering typologies has shown in another way the utility of the preventive measures put in place to counter money laundering. The analysis and discussion of methods and trends in virtually all FATF member countries began with analysis of suspicious transaction reports. These systems, implemented to help detect individual instances of money laundering have now become the starting point for examining the phenomenon from a more strategic point of view. Given the insight that this source of information provides to the state of money laundering in a particular jurisdiction, this use of STRs is an encouraging development.

10 February 1999

ANNEX TO THE 1998-1999 FATF REPORT ON MONEY LAUNDERING TYPOLOGIES

Selected cases of money laundering

Case Nº 1

Accounting firm

Facts

Beginning in May 1994, two alleged narcotics traffickers used an accounting firm to launder criminal proceeds generated from amphetamine sales. The 'clients' of the firm would on a regular basis hand their accountant cash in brown envelopes or shoe boxes for which no receipt was issued. The funds were then stored in the accountant's office until he decided how they could be introduced into the financial system and laundered. At any one time, there were between USD 38,000 and USD 63,000 stored in the accountant's office.

The law enforcement agency investigating the matter found that the accountant established company and trust accounts on behalf of his clients and opened personal bank accounts in the names of relatives. He then made structured deposits to those accounts with the funds received from the alleged traffickers. Additionally, he transferred approximately USD 114,000 overseas — again, using structured transactions — to purchase truck parts, which were later brought back into the country and sold at a profit, and also used some of the funds to purchase properties. The accountant and three of his colleagues (who were also implicated in the scheme) reportedly laundered approximately USD 633,900 and received a 10% commission for his services.

Results

The accountant and his colleagues are believed to have acted from the beginning with the suspicion that the clients were involved in illegal activities. Even after obtaining further specific knowledge of his clients' involvement in narcotics trafficking, he and his associates allegedly continued to facilitate money laundering.

Lessons

This case highlights the key role that financial experts can play in the laundering of criminal proceeds. Many of the services provided (establishment of specialised accounts or business entities, making real estate investments) are potential money laundering mechanisms that may be beyond the abilities of the less sophisticated criminal.

Case Nº 2

Structuring scheme

Facts

This case came to the attention of the police through an informant. An individual residing in a small town deposited the equivalent of USD 1,038,354 over a three year period into three financial institutions. The institutions involved were two of the country's major banks and a credit union. Nearly 95% of the deposits were made in cash. The account holder into whose accounts the deposits were made was the citizen of a neighbouring country where there had been an outstanding arrest warrant against him since 1982.

During the investigation, it was determined that the employees of the financial institutions had been suspicious of the account activity. They had noticed, for example, that some deposits were made in brown paper bags through the night deposit drawer, yet they did not disclose this information to authorities. Funds deposited into the accounts were ultimately transferred to the account holder by his writing cheques on these accounts.

Results

Whether or not suspicious transactions were reported was unfortunately left to the discretion of the financial institution. In this case, the institution employees could not be found to have violated any rules. Due to a lack of vigilance on the part of financial institution employees, even to very obvious suspicious financial activity, an individual was able to launder a substantial sum of money.

Lessons

This example reinforces the need to ensure that financial institution employees know what sort of financial activities might be suspicious and thus worthy of reporting. This case illustrates the advantage of mandatory suspicious transaction reporting. Having such an obligation provides an additional incentive for financial institutions to ensure that their employees have thorough knowledge of what constitutes suspicious financial activity. Furthermore, once in place, mandatory suspicious transaction reporting serves as a deterrent for some of the relatively unsophisticated laundering schemes as described here.

Case Nº 3

Gold smuggling

Facts

In 1997, a financial intelligence unit (FIU) in country A received various suspicious transaction reports involving nationals from Scandinavian countries. These individuals were making large purchases of gold in their own names using cash in the currencies of their home countries. The transactions were conducted at various financial institutions in country A.

Initial examination of the disclosures indicated that the Scandinavian nationals had neither an official address nor any known legal activity in country A. Information obtained from police and FIUs in their countries of origin revealed that some of the participants in the scheme had outstanding arrest warrants for serious tax fraud. The individuals were suspected to have purchased gold in country A and elsewhere (where the value added tax rate on gold is lower). They then sold the gold in their home countries via various companies.

The suspicious transactions initially appeared to be separate incidents; however, they were grouped together based on such factors as profile of the participants, financial organisations target, and the dates of the transactions. At one of the bureaux de change where the transactions took place, examination of numerical sequence of exchange statements and gold sales invoices provided further information on the methods used by the Scandinavian nationals. For example, the suspects would sometimes conduct their transactions together, and at other times they split up their funds and conducted identical operations on the same day with a series of targeted financial institutions. The co-ordination among seemingly separate transactions seems to indicate that participants in the scheme were all likely couriers for the same organisation.

Results

Given the suspicious nature of this group transactions, the dossier was passed over to the public prosecutor in country A. The dossier also contributed useful evidence to ongoing investigations on the home countries of the suspects.

Lessons

Criminal organisations that are willing to devote the human resources to spreading their laundering operation over a larger geographic area are thus more likely to go undetected. This scheme would not have been detected if the various suspicious transaction reports could not have been brought together and compared. Likewise, the full picture of the scheme could not have been developed had there not been information sharing with foreign counterpart authorities.

Case Nº 4

Insurance polices and real estate

Facts

An insurance company informed an FIU that it had underwritten two life insurance policies with a total value of USD 268,000 in the name of two European nationals. Payment was made by a cheque drawn on the accounts of a brokerage firm in a major EU financial market and a notary in the south-eastern region of the country.

The two policies were then put up as collateral for a mortgage valued at USD 1,783,000 that was provided by a company specialising in leasing transactions. As the policyholders did not pay in their own name, the issuer contacted the brokerage firm in order to discover the exact origin of the funds deposited in its account. It was informed that the funds had been received in cash and that the parties concerned were merely occasional clients.

The parties — two brothers — were known to a law enforcement agency through a separate investigation into the illegal import and export of classic automobiles. Moreover, two individuals with the same surname were suspected by the same agency of drug trafficking and money laundering.

Results

This case has not yet been passed to the prosecutorial authorities.

Lessons

This example shows the necessity for non-bank financial businesses (in this case insurance companies) to be aware of what constitutes suspicious financial activity. It also demonstrates the critical need for effective co-ordination between the information contained in suspicious transaction reports and law enforcement information.

Case Nº 5

Front companies

Facts

An FIU in country B received a report of a series of suspicious transactions involving the bank accounts of a West African citizen and his businesses, which specialised in industrial fishing. These accounts were opened in banks located in country B and consisted primarily of money changing operations. The businessman also owned several residences in his home country and in the capital region of country B. The companies that he jointly managed all had the same address in his home country.

The personal account of the West African businessman received a number of transfers from accounts in another European country and in his home country (over USD 2 million from 1995 to 1996). The business accounts of the companies received transfers from several business entities based in Europe which were ostensibly linked to fishing related activities (over USD 7 million from 1994 to 1997). The transfers out of the account (estimated at nearly USD 4 million over the same period) were made to various companies whose business was (according to official records) connected with maritime activity and to other individuals.

The FIU's analysis showed that the income of the West African companies concerned was grossly disproportionate to reported sales. In fact, the account transactions seemed to have little to do with industrial fishing (i.e., foreign currency sales, transfers from the bank accounts of European residents, transfers between the personal account of the West African businessman and his businesses, transfers between these businesses and those of Europe-based partners).

Furthermore, according to additional information received by the FIU, one of the partners of the West African businessman, a co-manager of one of the companies, was suspected of being involved in several financial offences in Italy. This individual reportedly had close associations with two Italian organised crime figures, and his Italian businesses have become the target of investigation into money laundering in

that country. Still another business partner of the West African businessman appears also to be involved in financial and fiscal offences.

Results

This case has not yet been passed to prosecutorial authorities.

Lessons

Given the unusual account transactions and the lack of a clear economic connections for some of the business activities, the operations described in this example very likely constitute a money laundering scheme to conceal the illegal sources of proceeds derived from various criminal activities. This case gives further support to the need for analysis of information from a variety of sources (suspicious transaction reports, financial institutions, company registries, police records, etc.) in order to gain a full picture of a complex laundering scheme.

Case Nº 6

Money transfers

Facts

In July 1997, the police arrested the leader of an Iranian drug trafficking group, suspect A, for possessing stimulants and other kinds of drugs. The subsequent investigation revealed that the suspect had remitted part of his illegal proceeds abroad.

A total of USD 450,000 was remitted via three banks to an account on behalf of suspect A's older brother B at the head office of an international bank in Dubai. Transfers were made on five occasions during the two months between April and June 1998 in amounts ranging from USD 50,000 to USD 150,000).

Another individual, suspect C, actually remitted the funds and later returned to Iran. On each occasion, C took the funds in cash to the bank, exchanged them for dollars, and then had the funds transferred. Each of the transactions took about one hour to conduct, and the stated purpose for the remittances was to cover 'living expenses'.

Results

Suspect A was initially charged with violating provisions of the anti-narcotics trafficking law. The money transfers revealed during the investigation led to additional charges under the anti-money laundering law. This was the first time that anti-money laundering provisions had been applied to the overseas transfers criminal proceeds. Court proceedings for this case are on-going.

Lessons

This case represents a classic example of a simple money laundering scheme and is also a good example of a case derived not just from suspicious transaction reporting but also as a follow-up to traditional investigative activity.

Case Nº 7

Offshore financial centres, solicitors, and other financial services providers

Facts

In December 1997, M-Bank, acting as an international clearing bank, received a wire transfer for USD 1.4 million that appeared to originate from a UK law firm. The transfer was to be credited to the account of 'AZ Brokerage International, Ltd.' in G-Bank.

Due to the initials used in the company's name, M-Bank suspected that AZ Brokerage International, Ltd. might be a controlled by Mr. 'AZ', who was known to be involved in dubious financial activities. The bank also knew that Mr. AZ had served two years in a foreign prison for his connections to a false monetary instrument scheme and that his personal assets were subject to bankruptcy proceedings.

M-Bank decided to make a suspicious transaction report to the FIU, and, at the same time, they informed G-Bank of their suspicion. G-Bank subsequently disclosed to the FIU that Mr. AZ was operating a number of accounts opened under the names of various companies, including AZ Brokerage International, Ltd.

Preliminary inquiries made by the FIU revealed, among other things, the following:

- A third financial institution, D-Bank, had submitted a report to the FIU a few weeks earlier. The report stated that D-Bank had concluded its banking relationship with Mr. AZ after having received several 'suspicious approaches' from him and from foreign sources.

- Mr. AZ appeared to be the principal of 20 legal entities registered in the national company registry. All of these business entities operated from his home address.

- The names of the businesses indicated involvement in various types of financial activity, such as 'AZ Fiduciary & Nominees', 'AZ Investment & Finance', 'AZ Insurance Guaranty Fund', etc.

- The holding company, AZ Holding, Ltd. was stated to have a fully paid share capital of 20 million USD confirmed by the company's state authorised accountant.

- None of the companies were licensed to provide any type of financial or brokering services in the country of registry, according to the financial supervisory authority.

The FIU requested that the banks disclose additional information on their banking relationship with Mr. AZ or legal entities controlled by him. G-Bank was further requested to freeze the amount of 1.4 million USD as soon as it was credited to the account controlled by Mr. AZ. This additional information revealed that a number of deposits had been made to the relevant accounts prior to the FIU disclosures. All deposits were made by international wire transfer, and the largest amounted to USD 1.5 million. Most of the funds received had been immediately used to purchase bank drafts that were sent to individuals and companies in the United Kingdom and the United States. It was also noted that the purpose of one wire transfer to a US law firm was stated as being a 'legal fee for establishment of AZ Merchant Bank'.

The above mentioned information was submitted to a criminal investigation team, and the next day Mr. AZ requested that G-Bank transfer several hundred US dollars to an offshore bank account in the name of an individual. The transaction was stopped, and Mr. AZ was arrested as he was due to depart on holiday to the Caribbean where he had planned to meet with several apparently associated individuals.

Documents subsequently seized provided the following information:

- The stated share capital of AZ Holding, Ltd. was based on a Certificate of Deposit with the face value of USD 20 million and issued by a Panamanian financial institution.

- Mr. AZ, in addition to the business entities registered in his country, also held beneficial and formal positions in a number of business entities incorporated in several offshore jurisdictions, including 'AZ Private Bank, Ltd.' registered in Antigua.

- The name of the above mentioned 'AZ Merchant Bank, Inc.' had been changed to 'AZ Banque de Commerce, Inc.' on the advice of the solicitor that later arranged for US incorporation.

- Mr. AZ claims to provide various types of financial services, including private banking and issue of 'proof of funds' for use in various types of high-yield investment programmes, etc.

- A large number of foreign clients — mainly from Eastern Europe and the United States — had made the initial payment in amounts between USD 5,000 and USD 50,000 to get access to his services.

After the arrest of Mr. AZ, the investigation team was contacted and later visited by several individuals who claim to represent the beneficiaries of three of the deposits amounting to nearly USD 3.5 million— including USD 1.6 million that had been frozen. However, no beneficial party was prepared to make a formal statement or to provide documentary evidence of the source of the funds. No formal claims for the release of the seized funds had been received eleven months after the investigation began.

Results

Mr. AZ was released from custody during the on-going investigation. It appeared, however, that he immediately resumed the same business upon his release. The investigative authority has recently requested the assistance of foreign law enforcement authorities in their investigation regarding USD 20 million that had been transferred from an offshore financial centre to the account of one of Mr. AZ's companies.

Lessons

This case illustrates how financial services providers operating in one country or through an offshore financial centre may facilitate money laundering, as well as legitimate business transactions. With any one jurisdiction having only one part of the picture, it is difficult to determine exactly how the whole scheme works. The fact that, after blocking the transfer of funds for eleven months, there were still no concrete claims from the beneficial owners for their return is also a further indication that the funds may not have been of strictly legal origin. This case is also a good example of how financial institutions can work with each other and anti-money laundering authorities to pull together a picture of the suspected laundering scheme.

Case Nº 8

Front companies, insurance, and bureaux de change

Facts

An FIU received a suspicious transaction report from an insurance company that specialised in life insurance. The report referred to Mr. H, born and resident in a Latin American country, as having recently taken out 'two sole premium life insurance policies for a total amount of USD 702,800'. Subsequent information provided to the FIU indicated that the policies premiums had been paid with two personal cheques made out by a third party and drawn against a major bank. The third party, Mr. K, was also a resident in the same Latin American country although not a national of that country. Further

checks at Mr. K's bank revealed that both he and Mr. H had signature authority on two business accounts, Sam, Ltd. and Dim, Ltd.

Examination of the accounts showed, especially in Mr K's account, that transactions were carried out on behalf of Mr H. Thus, the account had received funds from abroad and had also been used for other financial products besides the life insurance policies. Indeed, ten cheques in US dollars drawn against American banks and issued by two bureaux de change operating out of the Latin American country where the two men resided, had been deposited into Mr K's account. The value of these cheques totalled USD 1,054,200.

This activity appeared to show that the funds had been used to pay the insurance premium on Mr. H's life and to acquire stakes in investment funds, also for Mr. H, amounting to another USD 210,840. There were also other related transactions in the accounts of the two companies and Mr H's personal account. Cash or cheque transactions for amounts between USD 14,000 and USD 70,000 were among the related transactions. In one instance, a cheque was drawn of the Sam, Ltd. account for USD 63,300 on the day following the deposit of USD 70,280 in cheques into Mr K's account.

Checks into the backgrounds of Mr. H and Mr. K revealed that Mr. H was suspected of being involved in cocaine trafficking in Latin America. Mr. K had some minor violations (writing bad cheques, etc.); however, he had no serious criminal background. The business activities and backgrounds of Sam, Ltd. and Dim, Ltd. were also looked at. In both instances, the companies had been incorporated with a stock capital of USD 36,400 in which Mr. H and Mr. K had a 50% interest and were joint directors. Queries made at the 'Balance of Payments Office' as to foreign collection and payment revealed a total absence of operations in the previous two financial years.

Result

It appeared, therefore, that Mr. K was being used as the front man for Mr. H's efforts to move funds out of his country of residence. For greater security of the scheme, firms under their control were established that did not perform any corporate or commercial activity. Mr. H received the funds deposited in Mr. K's account through the sole premium insurance policies and shares in investment funds that had been paid for by that account, as well as through indirect income from the companies mentioned. In this case, the FIU believed there to be sufficient signs of money laundering and therefore passed the matter on to prosecutorial authorities.

Lessons

This operation is interesting because it shows that payment instruments or third party involvement having no apparent economic relationship to the transaction are often a key indicator of suspicious activity. It is worth noting that Mr. K was obviously selected based on his lack of prior criminal record and his nationality so as to minimise suspicion. The activities of the front companies were also conducted in such a way as to give the appearance of transactions from corporate activities. The case also highlights the potential value of suspicious transaction reporting by insurance companies.

Case Nº 9

The derivatives market: a typology

The following typology is provided as an example of how funds could be laundered using the derivatives market.

In this method, the broker must be willing to allocate genuinely losing trades to the account in which criminal proceeds are deposited. Instead of relying on misleading or false documentation, the broker uses the genuine loss making documentation to be allocated to the detriment of the dirty money account holder. As an example, a broker uses two accounts, one called 'A' into which the client regularly deposits money which needs laundering, and one called 'B' which is intended to receive the laundered funds. The broker enters the trading market and 'goes long' (purchases) 100 derivative contracts of a commodity, trading at an offer price of $85.02, with a 'tick' size of $25. At the same time he 'goes short' (sells) 100 contracts of the same commodity at the bid price of $85.00. At that moment, he has two legitimate contracts which have been cleared through the floor of the exchange.

Later in the trading day, the contract price has altered to $84.72 bid and $84.74 offered. The broker returns to the market, closing both open positions at the prevailing prices. Now, the broker, in his own books assigns the original purchase at $85.02 and the subsequent sale at $84.72 to account A. The percentage difference between the two prices is 30 points or ticks (the difference between $84.72 and $85.02). To calculate the loss on this contract, the tick size which is $25 is multiplied by the number of contracts, 100, multiplied by the price movement, 30. Thus: $25 x 100 x 30 = $75,000 (loss).

The other trades are allocated to the B account, which following the same calculation theory of tick size multiplied by the number of contracts multiplied by the price movement results in a profit as follows: $25 x 100 x 26 = $65,000 (profit). The account containing the money to be laundered has just paid out $75,000 for the privilege of receiving a profit of $65,000 on the other side. In other words, the launderer has paid $10,000 for the privilege of successfully laundering $75,000. Such a sum is well within the amount of premium which professional launderers are prepared to pay for the privilege of cleaning up such money. As a transaction, it is perfectly lawful from the point of view of the broker. He has not taken the risk of creating false documentation, which could conceivably be discovered, and everything has been done in full sight of the market.